



Financial Statements
June 30, 2020

South Dakota Retirement System,
South Dakota Retirement System
Supplemental Retirement Plan, and
South Dakota Retirement System
Special Pay Plan

**SOUTH DAKOTA RETIREMENT SYSTEM,
SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN,
SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN**

Table of Contents

South Dakota Retirement System

Independent Auditor's Report	1
Management's Discussion and Analysis	4
Financial Statements	
Statement of Fiduciary Net Position	8
Statement of Changes in Fiduciary Net Position	9
Notes to Financial Statements	10
Required Supplementary Information	
Schedule of Changes in the System's Net Pension Liability	32
Schedule of System's Net Pension Liability (Asset)	33
Schedule of System's Contributions	33
Schedule of Investment Returns	34
Notes to Schedules of Required Supplementary Information	35
Other Supplementary Information	
Schedule of Administrative Expenses	36
Schedule of Investment Activity Expenses	37
Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	38

South Dakota Retirement System Supplemental Retirement Plan

Independent Auditor's Report	40
Management's Discussion and Analysis	42
Financial Statements	
Statement of Fiduciary Net Position	46
Statement of Changes in Fiduciary Net Position	47
Notes to Financial Statements	48
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	55

South Dakota Retirement System Special Pay Plan

Independent Auditor's Report	57
Management's Discussion and Analysis	59
Financial Statements	
Statement of Fiduciary Net Position	63
Statement of Changes in Fiduciary Net Position	64
Notes to Financial Statements	65
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	70



Independent Auditor's Report

To the Board of Trustees
South Dakota Retirement System
Pierre, South Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the South Dakota Retirement System (SDRS), which comprise the statement of fiduciary net position as of June 30, 2020, and the related statement of changes in fiduciary net position, for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective statement of the fiduciary net position of the South Dakota Retirement System, as of June 30, 2020, and the respective statement of changes in fiduciary net position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 2 to the financial statements, the financial statements include investments valued at \$2,388,760,962 (19.43 percent of net position) whose carrying values have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on information provided by the fund managers or the general partners. Our opinion is not modified with respect to this matter.

Other Matters**Required Supplementary Information**

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the required supplementary information on pages 4-7 and 32-35 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise SDRS's basic financial statements as a whole.

The additional supplementary information listed as other supplementary information in the table of contents are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the accompanying financial information listed as supplemental schedules are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 4, 2020 on our consideration of SDRS's 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 solely 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 effectiveness of SDRS's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering SDRS's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "Eide Bailly LLP".

Boise, Idaho
November 4, 2020

SOUTH DAKOTA RETIREMENT SYSTEM

Management's Discussion and Analysis

June 30, 2020

This section presents management's discussion and analysis of the South Dakota Retirement System's (SDRS or the System) financial position and performance as of and for the year ended June 30, 2020. This section is intended to supplement the SDRS financial statements and should be read in conjunction with the remainder of the SDRS financial statements.

Financial Highlights

- The fiduciary net position of SDRS decreased by \$175 million during fiscal year 2020. This decrease was primarily due to the investment performance of 1.6 percent, which was below the assumed rate of 6.50 percent.
- SDRS paid \$602 million to SDRS benefit recipients in fiscal year 2020 compared to \$572 million in 2019.
- SDRS received \$263 million in SDRS member and employer contributions in fiscal year 2020 compared to \$255 million in 2019.

Overview of the Financial Statements and Accompanying Information

The basic financial statements consist of:

Financial Statements

The System presents the statement of the fiduciary net position as of June 30, 2020, and the statement of changes in fiduciary net position for the year then ended. These statements reflect resources available for the payment of benefits as of the year-end and sources and uses of those funds during the year.

Notes to Financial Statements

The notes to financial statements are an integral part of the financial statements and provide additional detailed information and schedules. Information in the notes provides disclosures concerning SDRS's organization, contributions and reserves, investments, the use of derivatives and securities lending, and other information.

Supplemental Information

In addition to this discussion and analysis, the required supplemental information consists of four schedules of trend data and related notes concerning the funded status of SDRS, changes in net pension liability (asset), investment returns, actuarial assumptions, and employer contributions.

Other supplementary schedules include detailed information on administrative expenses incurred by SDRS and a breakout of investment manager fees.

Financial Analysis

SDRS is a cost-sharing, multiple-employer public employee retirement system. SDRS provides retirement, disability, and survivor benefits for employees of the state of South Dakota and its political subdivisions. The benefits are funded through member and employer contributions and investment income.

SDRS benefits are based on the members' final average compensation, their years of credited service, and a benefit multiplier.

SOUTH DAKOTA RETIREMENT SYSTEM

Management's Discussion and Analysis

June 30, 2020

A summary of the fiduciary net position is shown below:

Summary of Fiduciary Net Position

June 30, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Assets		
Cash and cash equivalents	\$ 5,660,120	\$ 7,488,388
Receivables	42,537,740	384,345,349
Investments, at fair value	12,262,719,601	12,344,910,568
Other assets	1,214,224	1,470,817
Total assets	<u>12,312,131,685</u>	<u>12,738,215,122</u>
Liabilities		
Accounts payable and accrued expenses	2,530,060	2,115,371
Unsettled investment purchases	12,263,398	263,300,094
Total liabilities	<u>14,793,458</u>	<u>265,415,465</u>
Net position restricted for pension benefits	<u>\$ 12,297,338,227</u>	<u>\$ 12,472,799,657</u>

Change in Fiduciary Net Position

Additions to the fiduciary net position include member and employer contributions and net investment income. The fixed member and employer contribution rates are established by law. On an annual basis, an actuarial valuation of SDRS is made to determine the adequacy of the fixed contribution rates to pay the normal cost of benefits, expenses, and amortize the unfunded actuarial accrued liability. In addition to the fixed contributions, members and employers may make additional contributions to purchase uncredited prior service. These purchase or acquisition payments are also included as contributions.

Income from investments is the other primary source of revenue for SDRS. The actuarial assumed investment rate was 6.5 percent at June 30, 2020. The net investment returns were 1.6 percent for 2020 and 4.9 percent for 2019.

Deductions from fiduciary net position are primarily benefit payments. During 2020, SDRS paid \$602 million to benefit recipients or 5.2 percent more than 2019. The increase is due to the annual cost-of-living adjustment, which was 2.03 percent for fiscal year 2020, and additional annuitants. Refunds of accumulated contributions during 2020 decreased 2.7 percent. Administrative costs of SDRS increased 0.6 percent during 2020.

SOUTH DAKOTA RETIREMENT SYSTEM

Management's Discussion and Analysis

June 30, 2020

A summary of the changes in fiduciary net position is shown below:

Summary of Changes in Fiduciary Net Position

June 30, 2020 and 2019

	<u>2020</u>	<u>2019</u>	<u>Percentage change</u>
Additions			
Employee contributions	\$ 131,541,783	\$ 127,454,956	3.2%
Employer contributions	131,681,949	127,572,348	3.2%
Investment income	192,238,245	583,573,718	-67.1%
Total additions	<u>455,461,977</u>	<u>838,601,022</u>	<u>-45.7%</u>
Deductions			
Benefits	602,352,394	572,351,398	5.2%
Refunds of contributions	23,433,984	24,073,325	-2.7%
Administrative expenses	5,127,029	5,095,897	0.6%
Total deductions	<u>630,913,407</u>	<u>601,520,620</u>	<u>4.9%</u>
Net change in net position	(175,451,430)	237,080,402	-174.0%
Plan net position restricted for pension benefits			
Beginning of year	<u>12,472,799,657</u>	<u>12,235,719,255</u>	<u>1.9%</u>
End of year	<u>\$ 12,297,348,227</u>	<u>\$ 12,472,799,657</u>	<u>-1.4%</u>

Investments

SDRS investment portfolio management is the statutory responsibility of the South Dakota Investment Council. The South Dakota Investment Office is the primary investment manager, but the Investment Council may utilize the services of external money managers.

Net investment performance during 2020 and 2019 was 1.6 percent and 4.9 percent, respectively.

The Investment Council is governed by the prudent-man standard, as defined in South Dakota Codified Law §4-5-27:

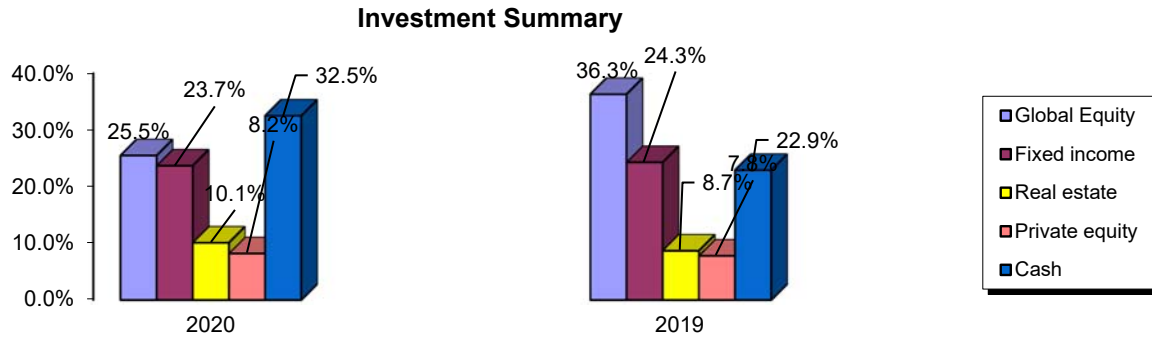
§4-5-27. Prudent-man standard required in investments. Any investments under the provisions of §4-5-12 to §4-5-39, inclusive, shall be made with the exercise of that degree of judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation but for investment, considering the probable safety of their capital as well as the probable income to be derived.

SOUTH DAKOTA RETIREMENT SYSTEM

Management's Discussion and Analysis

June 30, 2020

Though monthly benefit payments exceed monthly contributions, SDRS is not subject to sudden, substantial, and unexpected withdrawals. As a result, it is not necessary to maintain a high percentage of assets in short-term investments unless that is deemed to be the best investment strategy. This allows the SDRS trust fund to be fully invested in a diversified portfolio of securities.



Plan Status

While the markets have not always made it possible to achieve the long-term assumptions, the System's funding remains solid.

Requests for Information

Requests for information about SDRS may be directed to the South Dakota Retirement System at P.O. Box 1098, Pierre, SD 57501. You may also contact SDRS online at sdrs.sd.gov.

SOUTH DAKOTA RETIREMENT SYSTEM

Statement of Fiduciary Net Position

June 30, 2020

Assets	
Cash and cash equivalents	\$ 5,660,120
Receivables	
Employer	2,789,307
Employee	2,995,357
Benefits	146,115
Unsettled investment sales	10,596,146
Accrued interest and dividends	26,010,815
Total receivables	<u>42,537,740</u>
Investments, at fair value	
Equities	5,126,732,811
Fixed income	4,887,289,539
Real estate	1,245,732,639
Private equity	1,002,964,612
Total investments, at fair value	<u>12,262,719,601</u>
Assets used in plan operations, at cost (net of accumulated depreciation of \$865,249)	<u>1,195,352</u>
Other assets	<u>18,872</u>
Total assets	<u>12,312,131,685</u>
Liabilities	
Accounts payable and accrued expenses	2,530,060
Unsettled investment purchases	<u>12,263,398</u>
Total liabilities	<u>14,793,458</u>
Net position restricted for pension benefits	<u>\$ 12,297,338,227</u>

See accompanying notes to financial statements.

SOUTH DAKOTA RETIREMENT SYSTEM

Statement of Changes in Fiduciary Net Position

Year Ended June 30, 2020

Additions	
Contributions	
Employee	\$ 131,541,783
Employer	131,681,949
	<hr/>
Total contributions	263,223,732
	<hr/>
Investment Income	
From investing activities	
Net depreciation in fair value of investments	(36,540,901)
Interest	112,914,590
Dividends	143,214,987
Real estate	22,315,409
	<hr/>
Investment activity income	241,904,085
Less investment activity expenses	(50,396,397)
	<hr/>
Net investment activity income	191,507,688
	<hr/>
From security lending activities	
Security lending income	1,043,606
Security lending expenses	(313,049)
	<hr/>
	730,557
	<hr/>
Total additions	455,461,977
	<hr/>
Deductions	
Benefits	602,352,394
Refunds of contributions	23,443,984
Administrative expenses	5,127,029
	<hr/>
Total deductions	630,923,407
	<hr/>
Net change in net position	(175,461,430)
Net position restricted for pension benefits:	
Beginning of year	12,472,799,657
	<hr/>
End of year	\$ 12,297,338,227
	<hr/> <hr/>

See accompanying notes to financial statements.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(1) General Description of the System

The South Dakota Retirement System (SDRS or the System) is a cost sharing, multiple employer public employee retirement system (PERS) established to provide retirement benefits for employees of the state of South Dakota (the State) and its political subdivisions. Members of SDRS include full time employees of public schools, the State, the Board of Regents, city and county governments, and other public entities. Public schools, cities, and counties may choose not to include certain full time employees in the System.

SDRS is considered a part of the State financial reporting entity and is included in the State's financial report as a pension trust fund. Authority for establishing, administering, and amending plan provisions is found in South Dakota Codified Law (SDCL) 3-12C.

The South Dakota Retirement System Board of Trustees (the Board) is the governing authority of SDRS. The Board consists of 14 elected representatives from participating groups, two appointees of the governor, and an ex officio nonvoting representative of the South Dakota Investment Council. The elected representatives of the Board are two teacher members; two State employee members; a participating municipality member; a participating county member; a participating classified employee member; a current contributing Class B member other than a justice, judge, or magistrate judge; a county commissioner of a participating county; a school district board member, a justice, judge, or magistrate judge, an elected municipal official of a participating municipality; a retiree; and a faculty or administrative member employed by the Board of Regents. The two Governor's appointees consist of one head of a principal department established pursuant to SDCL 1-32-2, or one head of a bureau under the office of executive management and one individual from the private or public sector.

SDRS is a hybrid defined benefit plan designed with several defined contribution plan type provisions. The System includes three classes of members: Class A general members, Class B public safety and judicial members, and Class C Cement Plant Retirement Fund members. Members and their employers make matching contributions, which are defined in State statute. SDRS may expend up to 3 percent of the annual contributions for administrative expenses subject to approval by the executive and legislative branches of the State.

Members that were hired before July 1, 2017, are Foundation members. Class A Foundation members and Class B Foundation judicial members who retire after age 65 with three years of service are entitled to an unreduced annual retirement benefit. An unreduced annual retirement benefit is also available after age 55 for Class A Foundation members where the sum of age and credited service is equal to or greater than 85 or after age 55 for Class B Foundation judicial members where the sum of age and credited service is equal to or greater than 80. Class B Foundation public safety members can retire with an unreduced annual retirement benefit after age 55 with three years of contributory service. An unreduced annual retirement benefit is also available after age 45 for Class B Foundation public safety members where the sum of age and credited service is equal to or greater than 75. All retirement benefits that do not meet the above criteria may be payable at a reduced level. Class A and B eligible spouses of foundational members will receive a 60 percent joint survivor benefit when the member dies.

Members that were hired on/after July 1, 2017, are Generational members. Class A Generational members and Class B Generational judicial members who retire after age 67 with three years of contributory service are entitled to an unreduced annual retirement benefit. Class B Generational public safety members can retire with an unreduced annual retirement benefit after age 57 with three years of contributory service. At

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

retirement, married Generational members may elect a single-life benefit, a 60 percent joint and survivor benefit, or a 100 percent joint and survivor benefit. All Generational retirement benefits that do not meet the above criteria may be payable at a reduced level. Generational members will also have a variable retirement account (VRA) established, in which they will receive up to 1.5 percent of compensation funded by part of the employer contribution. VRAs will receive investment earnings based on investment returns.

Class C Cement Plant Retirement Fund members have a normal retirement age of 65 and early retirement is age 55 with the required credited service. Class C Cement Plant provides for disability payments for those disabled on or before March 16, 2001. All members of the Cement Plant Retirement Plan on March 15, 2001, were 100 percent vested. Class C members may elect a single-life benefit, or joint and survivor benefits as described in their plan documents.

Legislation enacted in 2017 established the current COLA process. At each valuation date:

- Baseline actuarial accrued liabilities will be calculated assuming the COLA is equal to the long-term inflation assumption of 2.25 percent.
- If the fair value of assets is greater or equal to the baseline actuarial accrued liabilities, the COLA will be:
 - * The increase in the 3rd quarter CPI-W, no less than 0.5 percent and no greater than 3.5 percent.
- If the fair value of assets is less than the baseline actuarial accrued liabilities, the COLA will be:
 - * The increase in the 3rd quarter CPI-W, no less than 0.5 percent and no greater than a restricted maximum such that, that if the restricted maximum is assumed for future COLAs, the fair value of assets will be greater or equal to the accrued liabilities.

All benefits except those depending on the Member's Accumulated Contributions are annually increased by the Cost-of-Living Adjustment.

SDRS is a qualified defined benefit retirement plan under Section 401(a) of the Internal Revenue Code and is exempt from federal income taxes. SDRS last received a favorable determination letter dated October 3, 2016, in which the Internal Revenue Service stated that the System, as then designated, was in compliance with the applicable requirements of the Internal Revenue Code. SDRS believes that the system currently is designed and being operated in compliance with the applicable requirements of the Internal Revenue Code, and therefore, SDRS continues to be tax-exempt as of June 30, 2020. Therefore, no provision for income taxes has been included in SDRS's financial statements.

SDRS is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. SDRS participates in the various programs administered by the State. These risk management programs are funded through assessments charged to participating entities. The risk management programs include (1) coverage for risks associated with automobile liability and general tort liability (including public officials' errors and omissions liability, medical malpractice liability, law enforcement liability, and products liability) through the State's Public Entity Pool for Liability Fund, (2) coverage of employee medical claims through the State's health insurance program, (3) coverage for unemployment benefits through the State's Unemployment Insurance

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

Fund, and (4) coverage for workers' compensation benefits through the State's Workers' Compensation Fund. Financial information relative to the self-insurance funds administered by the State is presented in the State of South Dakota Comprehensive Annual Financial Report.

As of June 30, 2020, the number of participating governmental employers is as follows:

School Districts	164
State of South Dakota	1
Board of Regents	1
Municipalities	168
Counties	65
Board and Commissions	101
	500
Total employers	500

At June 30, 2020, SDRS membership consists of the following:

Retirees and beneficiaries currently receiving benefits:	
Class A (general employees)	28,009
Class B (public safety and judicial employees)	1,924
Class C (cement plant employees)	234
	30,167
Total retirees and beneficiaries	
Terminated members entitled to benefits but not yet receiving them:	
Class A (general employees)	19,495
Class B (public safety and judicial employees)	1,128
Class C (cement plant employees)	32
	20,655
Total terminated members	
Current active members:	
Vested:	
Class A (general employees)	29,814
Class B (public safety and judicial employees)	2,438
Class C (cement plant employees)	12
Nonvested:	
Class A (general employees)	8,182
Class B (public safety and judicial employees)	879
	41,325
Total current active members	
Grand total	
92,147	

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

- * *There are 117 class A and 13 class B public safety and judicial members or beneficiaries whose benefits are currently suspended but are entitled to future benefits. These members or beneficiaries are included as retirees and beneficiaries in their respective classes as listed.*

(2) Summary of Significant Accounting Policies

(a) Basis of Accounting and Presentation

The accompanying financial statements are prepared using the accrual basis of accounting in accordance with U.S. generally accepted accounting principles applicable to governmental accounting for a pension trust fund. Employee and employer contributions are recognized when due pursuant to formal commitment, as well as statutory requirements. Pension benefit payments are due the first day of the month following the retirement of a member, and the first of each month thereafter. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

(b) Method Used to Value Investments

Investments are reported at fair value, in accordance with Governmental Accounting Standards Board (GASB) Statement No. 72. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GASB 72 sets forth the framework for measuring value. The framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels. The three levels of the fair value hierarchy under GASB 72 are described as follows:

Level 1 – Valuation inputs are quoted prices in active markets for identical asset or liability as of the measurement date.

Level 2 – Valuation inputs other than quoted prices included within Level 1 that are observable for an asset or liability, either directly or indirectly.

Level 3 – Valuation inputs are based on significant unobservable inputs for an asset or liability.

As a practical expedient, GASB 72 allows the net asset value (NAV) or its equivalent to be used when a readily determinable fair value is not available. The NAV valuations are based on valuations of the underlying companies as determined and reported by the fund manager or general partner and are excluded from the fair value hierarchy.

Additional required disclosures can be found in Note 5: Cash and Investments.

Investments denominated in foreign currencies are translated into United States Dollars (USD) using the year-end spot foreign currency exchange rates. Foreign exchange rate gains and losses are included with the net appreciation in fair value of investments.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

Alternative investments consist of investments in a variety of markets and industries through partnerships, corporate entities, co-investments, and other investment vehicles. For alternative investments where no readily ascertainable market value exists, management, in consultation with their investment advisors, values these investments in good faith based upon the investment's current financial statements or other information provided by the underlying investment advisor. For all of these alternative investments, SDRS has determined that net asset value reported by the underlying fund approximates the fair value of the investment. These fair value estimates are, by their nature, subjective and based on judgment. These alternative investments were valued at \$2,388,760,962 (19.43 percent of net position) at June 30, 2020. The estimated fair value of these investments may differ significantly from values that would have been used had a ready market existed.

Futures contracts are marked to market based on quoted futures prices with changes in fair value reflected in the current period.

Interest is accrued in the period in which it is earned and dividend income is recorded on the ex-dividend date.

The arithmetically calculated money-weighted return net of fees was 1.56 percent in 2020. The money-weighted rate of return considers the changing amounts actually invested during a period and weights the amount of pension plan investment by the proportion of time they are available to earn during that period. The rate of return equates the sum of weighted external cash flows into and out of pension plan investments to the ending fair value of the pension plan investment.

(c) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the plan administrator to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and changes therein. Actual results could differ from those estimates.

(3) Contributions

(a) Contributions

Covered employees are required by statute to contribute a percentage of their salary to SDRS as follows:

Class A members	6.0% of salary
Class B public safety members	8.0% of salary
Class B judicial members	9.0% of salary

All participating employers are required to contribute an amount equal to the members' contributions. Members may make an additional contribution of 1.5 percent of compensation for optional spouse coverage (closed to new enrollees after July 1, 2010).

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

SDRS is funded by fixed member and employer contributions at a rate established by South Dakota law. On an annual basis, an actuarial valuation of SDRS is performed to determine the adequacy of the fixed contributions to pay the normal costs and expenses, if the System is fully funded or pay the normal costs, expenses and amortize the unfunded actuarial accrued liability (UAAL) if the System is not fully funded. The June 30, 2020, actuarial valuation of the plan determined that the System is fully funded and that the statutorily required employer contributions meet the requirements for the annual required contributions of the employers under GASB Statement No. 67, *Financial Reporting for Pension Plans*; and the statutorily required employer contributions are sufficient to pay the employer normal cost and expenses. Annual required contributions of the employers equal to the statutorily required contributions have been listed below pursuant to GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*.

Contributions during fiscal year 2020 totaling \$263,223,732 (\$131,541,783 employee, \$131,681,949 employer) were made in accordance with statutory rates. The employer contributions exceed the employee contributions due to the effect of SDCL 3-12C-1405, which governs the contributions of retired members who enter covered employment. Contributions for the last 5 fiscal years are as follows:

	Employer	Percentage contributed
Year ending June 30:		
2020	\$ 131,681,949	100%
2019	127,572,348	100
2018	124,734,270	100
2017	121,907,646	100
2016	114,090,075	100

SDRS allows participating entities to pay their deferred contributions for funding of accrued benefits over periods of up to 20 years and members to pay for the purchase of certain prior service over periods of up to 10 years. Interest is charged at rates of 5 percent to 8 percent.

Future payments will be received as follows:

	Employees
Year ending June 30:	
2021	\$ 38,469
2022	65,096
2023	32,767
2024	26,591
2025	20,552
Later	55,226
Deferred contributions receivable at June 30, 2020	\$ 238,701

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(4) Net Pension Liability (Asset) of the System

The components of the net pension liability (asset) of the System at June 30, 2020, was as follows:

Total pension liability	\$12,292,995,247
Plan fiduciary net position	<u>(12,297,338,227)</u>
Net pension liability (asset)	<u>\$ (4,342,980)</u>

Fiduciary net position as a percentage of net pension liability	100.04%
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Actuarial Assumptions – The total pension liability was determined by an actuarial valuation as of June 30, 2020, using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.25%
Salary increases	6.50% at entry to 3.0% after 25 years of service
Discount Rate	6.50%, net of pension plan investment expenses
Future COLAS	1.41%

Mortality rates were based on 97 percent of the RP-2014 Mortality Table, adjusted to 2006 and projected generationally with Scale MP-2016, white collar rates for females and total dataset rates for males. Mortality rates for disabled members were based on the RP-2014 Disabled Mortality Table, adjusted to 2006 and projected generationally with Scale MP-2016.

The actuarial assumptions used in the June 30, 2020, valuation were based on the results of an actuarial experience study for the period of July 1, 2011, to June 30, 2016.

Discount rate – The discount rate used to measure the total pension liability was 6.50 percent. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that matching employer contributions will be made at rates equal to the member rate. Based on those assumptions, the pension plan’s fiduciary net position was projected to be available to make all future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of (asset)/liability to changes in the discount rate – The following presents the net pension (asset)/liability of the System, calculated using the discount rate of 6.50 percent, as well as what the System’s net pension (asset) liability would be if it were calculated using a discount rate that is 1 percent point lower (5.50 percent) or 1 percent point higher (7.50 percent) than the current rate:

	<u>1 percent Decrease</u>	<u>Current Discount Rate</u>	<u>1 percent Increase</u>
System’s net pension (asset)/liability	\$ 1,684,788,558	\$(4,342,980)	\$ (1,386,019,309)

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(5) Cash and Investments

Cash and Deposits

Cash and cash equivalents are held by the State Treasurer and were invested in the State's pooled investment fund. Investments in the State's pooled investment fund consist primarily of short-term U.S. Treasury and Agency obligations, short-term U.S. Corporate securities, bank certificates of deposit, and money market funds.

The custodial credit risk for deposits is the risk that, in the event of the failure of a depository institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are held in the possession of an outside party. SDRS has a formal deposit policy specific to custodial credit risk and foreign currencies. Policy states that the USD equivalent of any non-USD currency cannot exceed 2.0 percent of any portfolio on a trade date +7 days basis. All portfolios as of June 30, 2020 meet policy guidelines. These deposits are not collateralized or covered by depository insurance. As a result, \$7,270,496 was exposed to custodial credit risk, which is recorded in investments in the statement of fiduciary net position.

Investments

Investment portfolio management is the statutory responsibility of the South Dakota Investment Council (SDIC), which may utilize the services of external money managers for management of a portion of the portfolio. SDIC is governed by the Prudent Man Rule (i.e., the council should use the same degree of care as a prudent man). Current SDIC investment policies dictate limits on the percentage of assets invested in various types of vehicles (equities, fixed income securities, real estate, cash, private equity, etc.). The long-term expected rate of return on pension plan investments was determined using a method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighing the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2020, (see the discussion of the pension plan's investment policy) are summarized in the following table using geometric means:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Global Equity	58 percent	5.1 percent
Fixed Income	30 percent	1.5 percent
Real Estate	10 percent	6.2 percent
Cash	<u>2 percent</u>	1.0 percent
	100 percent	

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

Below is a detail of the investment balances and amounts managed by the respective fund managers:

	Cost	Fair value
State of South Dakota Investment Council	\$ 8,698,502,818	\$ 8,960,879,753
Ares	4,591,289	1,195,064
Blackstone Private Equity	194,301,981	218,835,044
Blackstone Real Estate Partners	807,410,112	884,323,756
Bridgewater Pure Alpha Fund II	36,742,005	80,893,231
Brookfield Strategic RE III	34,716,925	36,978,438
Capital International	41,328,138	40,276,057
Carlyle	77,069,623	115,019,794
Cinven	133,511,326	135,433,176
CVC	88,437,783	73,113,949
CVI Global Value Fund	17,579,616	3,288,047
Cypress Merchant Banking Partners LP	24,326	24,326
Dimensional Fund Advisors, Inc.	16,969,109	55,882,432
Doughty Hanson PE IV	3,806,350	1,744,352
Elevation Partners	272,338	80,698
Encap Energy	12,709,951	8,961,888
KKR Associates	834,840	360,479
Lone Star Real Estate	113,482,026	95,833,492
Pinebridge	3,478,984	3,012,941
Riverstone	159,734,888	67,028,169
Rockpoint RE IV	118,741,639	122,063,802
Sanders Capital	84,427,892	98,159,841
Silver Lake	232,999,613	339,073,738
Starwood RE IX	114,111,721	105,338,088
TCW Opp MBS Strategy	764,394,864	814,919,046
Total	\$ 11,760,180,157	\$ 12,262,719,601

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(a) Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The investment grade fixed income portfolios of SDRS are benchmarked to the duration of the Citigroup Broad Investment Grade (BIG) Index and must fall between 70 percent and 130 percent of the BIGs duration.

The durations of the various investment types are listed in the following table:

	<u>Fair value</u>	<u>Duration (in years)</u>
Investment type:		
U.S. Treasury Bills	\$ 339,145,645	0.24
U.S. Treasury STRIPS	385,145,554	9.29
U.S. agencies	36,331,129	6.66
Investment grade corporates	441,063,845	4.26
High-yield corporates	399,538,768	3.34
Agency mortgage-backed securities	336,055,907	2.99
Non-agency mortgage-backed securities	777,464,377	0.67
Total	<u>\$ 2,714,745,225</u>	3.18

The SDRS fixed income portfolios invest in mortgage-backed securities. These securities are sensitive to prepayments by mortgagees, which is likely in declining interest rate environments, thereby reducing the value of these securities.

(b) Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to SDRS. SDIC sets the investment policy annually for the SDRS. This policy establishes the average percentage invested in each asset category and the fund allocation range that each asset category can vary during the fiscal year. As of June 30, 2020, the portfolios held the following investments, excluding those issued by or explicitly guaranteed by the U.S. government, which are not considered to have credit risk. The investments are grouped as rated by Moody's Investors Service.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

	<u>Fair value</u>
Moody's rating:	
Aaa	\$ 2,356,748,247
Aa	132,463,163
A	149,011,261
Baa	199,510,610
Ba	190,972,446
B	265,029,235
Caa	182,513,335
Ca	161,707,195
C	22,620,417
Unrated	289,591,012
Total	<u>\$ 3,950,166,921</u>

(c) Concentration of Credit Risk

Concentration of credit risk is the risk of loss that may be attributed to the magnitude of SDRS's investment in a single issuer. SDRS does not have guidelines to limit its investments in any particular investment. SDRS does not have investments in any one issuer that represent 5 percent or more of the total fair value of investments as of June 30, 2020 (excluding those issued by or explicitly guaranteed by the U.S. government).

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(d) Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely impact the fair value of an investment. SDRS's exposure to foreign currency risk derives from its positions in foreign currency and foreign-currency-denominated equity and fixed income investments. SDRS does not hedge foreign currency back to U.S. dollars (to match the unhedged benchmark), but does allow hedging under certain circumstances, when deemed appropriate. The portfolio's exposure to foreign currency risk at June 30, 2020, is as follows (in U.S. dollar fair value):

	Equities	Cash	Total
Currency:			
Australian Dollar	\$ 13,771,186	\$ 275,608	\$ 14,046,794
British Pound	145,830,805	1,565,746	147,396,551
Canadian Dollar	54,559,839	946,850	55,506,689
Danish Kroner	11,540,747	12,663	11,553,410
Euro	349,805,758	2,119,787	351,925,545
Hong Kong Dollar	10,880,318	69,279	10,949,597
Japanese Yen	169,405,370	2,264,402	171,669,772
Korean Won	75,306,542	-	75,306,542
Norwegian Krone	1,080,056	16,141	1,096,197
Singapore Dollar	1,193,053	-	1,193,053
Swedish Krona	6,726,312	-	6,726,312
Swiss Franc	171,226,608	20	171,226,628
Thai Baht	1,156,084	-	1,156,084
Total fair value	\$ 1,012,482,678	\$ 7,270,496	\$ 1,019,753,174

Investments with limited partnerships and certain global equity investments with external managers, which are not included in the table above, may expose SDRS's portfolio to additional foreign currency risk. The total fair value of investments in real estate and private equity limited partnerships as of June 30, 2020, was \$2,248,697,251. The total fair value of global equity and high-yield fixed income investments managed by external managers was \$55,882,432 and \$3,288,047, respectively.

(e) Return on Investments

During fiscal year 2020, SDRS's investments (including investments bought and sold, as well as held during the year) depreciated in value by \$36,540,901.

The calculation of realized gains and losses is independent of a calculation of the net change in the fair value of investments. Realized gains and losses on investments that had been held in more than one fiscal year and sold in the current year were included as a change in the fair value of investments reported in the prior years and current year.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

Change in Fair Value of Investments

Appreciation (Depreciation) in fair value of investments:	
Equities	\$ (568,463,485)
Fixed income	(102,519,326)
Real estate	(90,477,468)
Private equity	(77,719,037)
Change in accrued income	<u>(11,671,939)</u>
Total decrease in fair value	<u>(850,851,255)</u>
Realized gain (loss) on investments:	
Equities	282,037,253
Fixed income	(1,745,876)
Real estate	55,791,315
Private equity	<u>23,907,970</u>
Total net realized gains	<u>359,990,662</u>
Futures - change in unrealized gain	12,536,001
Futures - Realized gain	<u>441,783,691</u>
Net gain on futures	<u>454,319,692</u>
Net depreciation in investments	<u><u>\$ (36,540,901)</u></u>

(f) *Securities Lending*

State statutes and SDRS policies permit the use of investments for securities lending transactions. These transactions involve the lending of corporate debt, foreign equity securities, and domestic equity securities to broker-dealers for collateral in the form of securities, with the simultaneous agreement to return the collateral for the same securities in the future. SDRS's securities custodian is an agent in lending securities and shall accept only U.S. government securities or its agencies as collateral for any loan or loaned securities. The collateral required must equal 102 percent of fair value plus accrued interest for corporate debt securities, 102 percent of fair value for U.S. equity securities, and 105 percent of fair value for foreign securities except in the case of loans of foreign securities, which are denominated and payable in U.S. dollars, in which event the collateral required is 102 percent of fair value. The earnings generated from the collateral investments result in the gross earnings from lending activities, which is then split on a percentage basis with the lending agent.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

The fair value of securities on loan as of June 30, 2020, was \$195,997,176 and the collateral held on the same date was \$200,786,574. SDRS has no credit risk exposure to borrowers because the amounts the SDRS owes the borrowers exceed the amounts the borrowers owe SDRS. The contract with the lending agent requires the agent to indemnify SDRS if the borrowers fail to return the loaned securities and the collateral is inadequate to replace the securities lent.

All securities loans can be terminated on demand by either SDRS or the borrower. SDRS does not have the ability to pledge or sell collateral securities unless the borrower defaults; therefore, no asset and corresponding liability for the collateral value of securities received has been established on the statement of fiduciary net position. Regarding restrictions on loans, the securities lending agreement does limit the total value of securities that can be out on loan on any given day.

(g) *Custodial Credit Risk*

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. SDRS securities lending policies are detailed in the preceding Securities Lending section. As of June 30, 2020, the SDRS does not have custodial credit risk with regard to the security lending collateral.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(h) Fair Value Measurements and Applications

The following table shows the fair value in accordance with the GASB hierarchy:

Investments Measured at Fair Value	6/30/2020	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Fixed Income Securities				
US Treasury Bills	\$ 339,145,645	\$ -	\$ 339,145,645	\$ -
US Treasury STRIPS	385,145,554	-	385,145,554	-
US agencies	36,331,129	-	36,331,129	-
Investment grade corporates	441,063,845	-	441,063,845	-
High-yield corporates	399,538,768	-	399,538,768	-
Agency Mortgage-backed securities	336,055,907	-	336,055,907	-
Non-Agency Mortgage-backed	777,464,377	-	777,464,377	-
Total Fixed Income Securities	2,714,745,225	-	2,714,745,225	-
Equity Securities				
Domestic Stock	3,440,603,054	3,440,557,346	45,708	-
Depository Receipts	58,763,583	58,763,583	-	-
ETF - Exchange Traded Fund	588,403,820	588,403,820	-	-
International Stock	1,012,482,678	1,012,482,678	-	-
Stock Rights	1,625,463	1,625,463	-	-
Stock Warrants	59,559	59,559	-	-
Total Equity Securities	5,101,938,157	5,101,892,449	45,708	-
Total investments by fair value level	\$ 7,816,683,382	\$ 5,101,892,449	\$ 2,714,790,933	\$ -
Investments Measured at Net Asset Value (NAV)				
Short Term Investment Funds	2,049,158,139			
Emerging Markets Small Cap Equity Mutual Funds	55,882,432			
Multi-Strategy Hedge Funds	80,893,231			
Alternative Investments				
Real Estate Funds	1,245,732,639			
Private Equity Funds	1,002,964,612			
Other Funds	3,288,047			
Total alternative investments	2,251,985,298			
Investments, Measured at NAV	\$ 4,437,919,100			
Total Investments measured at fair value	\$ 12,254,602,482			
Plus: cash Held by Fund Managers	7,436,939			
Less: GL of FX Transactions	(59,821)			
Plus: Accrued Interest Purchased	931,505			
Less: Accrued Monthly Interest	(191,504)			
	\$ 12,262,719,601			
Investment derivative instruments				
Foreign Exchange Forward Contracts (liability)	(59,821)	-	(59,821)	-
Total investment derivative instruments	\$ (59,821)	\$ -	\$ (59,821)	\$ -

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

Equity securities classified in Level 1 of the fair value hierarchy are valued using quoted prices in active markets for identical securities as of the measurement date as issued by pricing vendors. Securities classified in Level 2 of the fair value hierarchy include valuations using quoted prices for a similar security in active markets, and valuations from various pricing vendors/brokers using observable inputs other than quoted prices for identical securities.

Debt securities classified in Level 2 of the fair value hierarchy are valued using observable inputs other than quoted prices for identical securities. The prices are determined by the use of matrix pricing techniques maintained by various pricing vendors/brokers for these securities. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices.

Real estate funds classified in Level 3 of the fair value hierarchy are real estate alternative investments that invest primarily in overseas commercial real estate. These are investments which quoted prices are not readily available and are valued at estimated values as determined by the General Partner (GP). Investments are valued by the GP using one or more valuation methodologies with reference to the International Private Equity and Venture Capital Valuation Guidelines. The estimated fair values are subjective and based on judgment.

SDRS holds shares or interest in investments where the fair value of the investments are measured on a recurring basis using net asset value per share (or its equivalent) of the investment as a practical expedient. The NAV valuations are based on valuations of the underlying companies as determined and reported by the fund manager or general partner.

Derivative instruments classified in Level 2 of the fair value hierarchy are valued using observable inputs other than quoted prices for identical securities. The foreign currency forward contract valuations are determined by interpolating FX rates for various settlement dates as of June 30, 2020.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

The valuation method for investments measured at the net asset value (NAV) per share (or its equivalent) is presented in the following table:

<u>Investments Measured at Net Asset Value (NAV)</u>		<u>Unfunded Commitments</u>	<u>Redemption Frequency (if currently eligible)</u>	<u>Redemption Notice Period</u>
Short Term Investment Funds (a)	\$ 2,049,158,139		Daily	0 days
Emerging Markets Small Cap Equity Mutual Funds (b)	55,882,432		Daily	1 day
Multi-Strategy Hedge Funds (c)	80,893,231		Monthly	5-30 days
Alternative Investments				
Real Estate Funds (d)	1,245,732,639	1,166,194,615		
Private Equity Funds (e)	1,002,964,612	508,506,435		
Other Funds (f)	<u>3,288,047</u>			
Investments, Measured at net asset value (NAV)	<u>\$ 4,437,919,100</u>			

(a) Short Term Investment Funds. This type includes investments in four open-end mutual funds that invest exclusively or primarily in high-quality, short-term securities that are issued or guaranteed by the U.S. government or by U.S. government agencies and instrumentalities. The fair values of the investments in this type have been determined using the NAV per share of the investments.

(b) Emerging Markets Small Cap Equity Mutual Funds. This type includes one investment in an open-end mutual fund that emphasizes broad diversification and consistent exposure to emerging market small company stocks. The fair value of the investment in this type has been determined using the NAV per share of the investment.

(c) Multi-Strategy Hedge Funds. This type includes two investments in funds that may invest in a wide range of asset classes in order to meet fund objectives. The fair values of the investments in this type have been determined using the NAV per share of the investments.

(d) Real Estate Funds. This type includes 26 real estate funds that invest primarily in commercial real estate. The fair values of the investments in this type have been determined using the NAV per share (or its equivalent) of the portfolio's ownership interest in partners' capital. These investments can never be redeemed from the funds. Distributions from each fund will be received as the underlying investments of the funds are liquidated. It is expected that the underlying assets of the funds will be liquidated over the next 20 years. Because it is not probable that any individual investment will be sold, the fair value of each individual investment has been determined using the NAV per share (or its equivalent) of the portfolio's ownership interest in partners' capital.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(e) Private Equity Funds. This type includes 35 private equity funds that invest primarily in leveraged buyouts. The fair values of the investments in this type have been determined using the NAV per share (or its equivalent) of the portfolio's ownership interest in partners' capital. These investments can never be redeemed from the funds. Distributions from each fund will be received as the underlying investments of the funds are liquidated. It is expected that the underlying assets of the funds will be liquidated over the next 20 years. Because it is not probable that any individual investment will be sold, the fair value of each individual investment has been determined using the NAV per share (or its equivalent) of the portfolio's ownership interest in partners' capital.

(f) Other Funds. This type includes two other alternative investments that invest primarily in a broad range of debt, debt-related, and/or real estate-related investments. The fair values of the investment has been determined using the NAV per share (or its equivalent) of the portfolio's ownership interest in partners' capital. This investment can never be redeemed from the funds. Distributions from the fund will be received as the underlying investments of the funds are liquidated. It is expected that the underlying assets of the fund will be liquidated over the next 2 years. Because it is not probable that any individual investment will be sold, the fair value of each individual investment has been determined using the NAV per share (or its equivalent) of the portfolio's ownership interest in partners' capital.

(6) Derivatives

Derivatives are generally defined as contracts whose values depend on, or derive from, the value of an underlying asset, reference rate, or index. SDRS is exposed to various derivative products through the investment management of the SDIC and its external managers. All of SDRS's derivatives are classified as investment derivatives.

Futures Contracts

A futures contract is a contract to buy or sell units of an index or financial instrument at a specified future date at a price agreed upon when the contract is originated. The South Dakota Investment Council purchases and sells futures contracts as a means of adjusting the SDRS portfolio mix at a lower transaction cost than the transactions, which would otherwise occur in the underlying portfolios. During fiscal year ended June 30, 2020, S&P 500 futures and 10-year U.S. Treasury note futures were utilized. Upon entering into such a contract, SDRS pledges to the broker cash or U.S. government securities equal to the minimum initial margin requirement of the futures exchange. Additionally, SDRS receives or pays a daily variation margin, which is an amount of cash equal to the daily fluctuation in value of the contract. The change in fair value of the futures contracts is presented in the statement of changes in fiduciary net position as "Net appreciation in fair value of investments." The net change in fair value from futures contracts for fiscal year ended June 30, 2020 was \$454,319,692.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

Futures contract positions at June 30, 2020 were as follows:

Description	Expiration date	Open position	Number of contracts	Notional Contract size	Fair value
U.S. Treasury note	September 2020	Long	4,325	100,000 par value 6%, 10-year U.S. Treasury note	\$ 370,893,047
S&P 500 Index	September 2020	Short	13,436		\$ (2,076,029,950)

Foreign Currency Forward Contracts

The SDIC enters into foreign exchange forward contracts for SDRS to manage foreign currency exposure, as permitted by portfolio policies. The fair values of the contracts are presented in the Statement of Fiduciary Net Position as Investments, at fair value – Equities. The change in fair value of the forward contracts is presented in the statement of changes in fiduciary net position as “Net appreciation in fair value of investments.” The net change in fair value from foreign currency forward contracts for fiscal year ended June 30, 2020 was \$449,350. At June 30, 2020, the foreign currency forward contracts outstanding were as follows:

Description	Notional amount	Currency	Value date	Fair value (US dollars)
Forward sale	\$ (4,247,124)	CHF	8/5/2020	\$ (59,821)

(a) Credit Risk

SDRS is exposed to credit risk on derivative instruments that are in asset positions. The SDIC attempts to minimize credit risk by entering into derivatives contracts with major financial institutions. At June 30, 2020, the net fair value of foreign currency forward contracts was \$0. This represents the maximum loss that would be recognized at the reporting date if all counterparties failed to perform as contracted.

(b) Foreign Currency Risk

SDRS is exposed to foreign currency risk on its foreign currency forward contracts because they are denominated in foreign currencies. The net fair value of the foreign currency forward contracts in U.S. dollars is \$(59,821).

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(7) Compensated Absences

Annual leave is earned by all SDRS employees. Upon termination, SDRS employees are eligible to receive compensation for their accrued annual leave balances. At June 30, 2020, a liability existed for accumulated annual leave calculated at the employees' June 30, 2020 pay rate in the amount of \$203,977. Employees who have been continuously employed by SDRS and the State for at least seven years prior to the date of their retirement, voluntary resignation, or death will receive payment for one-fourth of their accumulated sick leave balance with such payment not to exceed the sum of 12 weeks of the employee's annual compensation. For employees who have not been employed for seven continuous years, an accrued liability is calculated assuming the likelihood that they will meet the seven-year threshold in the future. At June 30, 2020, a liability existed for accumulated and accrued sick leave calculated at the employees' June 30, 2020 pay rate in the amount of \$188,321.

	2020	2019	Percentage change
Total compensated absences	\$ 392,298	\$ 382,314	2.61%

The total leave liability for the current year is on the statement of fiduciary net position available for benefits in accounts payable and accrued expenses.

(8) Operating Leases

SDRS has entered into an agreement to lease office space effective June 2020 and has a term of ten years. A schedule of minimum office rental payments as of June 30, 2020, is as follows for the fiscal years ending June 30:

2021	\$	156,128
2022		156,128
2023		156,128
2024		156,128
2025		156,128
Thereafter		780,640
Total remaining minimum payments	\$	1,561,280

Lease expense for the year ending June 30, 2020 was \$112,279.

(9) Supplemental Retirement Plan

SDRS offers a deferred compensation plan known as the Supplemental Retirement Plan (SRP), created in accordance with Internal Revenue Code Section 457. SRP is available to all public employees and permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseen emergency.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

All amounts of compensation deferred under the SRP, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are at all times held in trust for the exclusive benefit of the participants until made available to a participant or the participant's beneficiary.

Of the \$450,791,901 net position restricted for plan benefits at June 30, 2020, \$269,783,632 was held in trust for employees of the State, while the remaining \$181,008,269 represents the assets held in trust for employees of other jurisdictions. In order to avoid duplication in reporting, the SDRS total of \$2,673,284 is included in the State total and the State's comprehensive annual financial report for the year ended June 30, 2020.

(10) Special Pay Plan

The Special Pay Plan (SPP) was established in July 2004 as a qualified plan pursuant to Internal Revenue Code Section 401(a) under the administrative responsibility of the SDRS Board of Trustees. South Dakota state government and the South Dakota Board of Regents are participating units and every state political subdivision may become a participating unit in the plan. The SPP mandates that qualifying employees (over age 55 and \$600 or more in special pay) of participating units defer 100 percent of their special lump-sum termination pay to the plan. The participating unit transfers the deferred pay to the fund. This deferred pay is available to a participant immediately after termination, upon later retirement, or to beneficiaries or an estate upon the participant's death.

Of the \$65,261,670 net position restricted for plan benefits at June 30, 2020, \$35,296,499 was held in trust for employees of the State, while the remaining \$29,965,171 represents the assets held in trust for employees of other jurisdictions. In order to avoid duplication in reporting, the SDRS total of \$98,052 is included in the State total and the State's comprehensive annual financial report for the year ended June 30, 2020.

(11) Plan Termination

SDRS is administered in accordance with South Dakota statutes. The statutes provide for full vesting in accrued benefits upon termination of the plan (SDCL 3-12C-221).

(12) Commitments

At June 30, 2020, SDRS had uncalled capital commitments to private equity limited partnerships totaling approximately \$817,668,688 and to real estate limited partnerships totaling approximately \$1,166,194,615. The commitments may be called at the discretion of the general partner or may never be called.

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Financial Statements

June 30, 2020

(13) Litigation

Deutsche Bank and Wilmington Trust Company have filed a number of actions around the country against selling shareholders, and those actions are all consolidated in a Multi District Panel proceeding in the Southern District of New York (In re: Tribune Company Fraudulent Conveyance Litigation, Case No. 11-MD-2296). A separate adversary proceeding which was pending in Delaware has been consolidated into this action as well (The Official Committee of Unsecured Creditors of Tribune Company, on behalf of Tribune Company v. Dennis J. FitzSimmons, et al., Case No. 1:12-cv-02652). SDRS is a defendant as a result of selling Tribune Stock in connection with a leveraged buyout of the Tribune Company in 2007. The creditors of Tribune Company are attempting to claw-back funds received in connection with the sale of the stock, which, in the case of SDRS, is approximately four million dollars. All claims against the former Tribune shareholders (defendants) have been dismissed. The FitzSimmons litigation was dismissed in January 2017; however, there is an ongoing appeal in the Second Circuit. The Noteholder litigation was dismissed in 2013 and affirmed by the Second Circuit. The Noteholders sought review by the U.S. Supreme Court and the shareholders are currently opposing Noteholders' petition for writ of certiorari. The pending legal action does not represent an immediate negative contingency.



Required Supplementary Information
June 30, 2020

South Dakota Retirement System

SOUTH DAKOTA RETIREMENT SYSTEM

Schedules of Required Supplementary Information

June 30, 2020

SCHEDULE OF CHANGES IN THE SYSTEM'S NET PENSION LIABILITY

Last Fiscal Year

	2020	2019	2018	2017	2016	2015	2014
Total pension liability							
Service cost	\$ 237,264,711	\$ 233,802,396	\$ 222,709,592	\$ 192,682,191	\$ 184,923,317	\$ 179,349,820	\$ 161,697,696
Interest	805,447,155	791,288,656	752,702,794	781,413,919	745,774,586	712,632,857	633,951,211
Changes in benefit terms	2,246,202	-	-	(567,079,980)	-	-	(5,082,771)
Differences between expected and actual experience	6,447,338	(6,190,846)	5,220,615	97,593,700	78,645,840	55,821,847	78,328,269
Changes of assumptions	(594,816,177)	(193,660,111)	181,931,669	820,191,401	-	-	604,281,184
Cement plant consolidation	-	-	-	-	-	-	60,649,185
Benefit payments, including refunds	(625,796,378)	(596,424,723)	(564,141,147)	(541,090,032)	(510,496,482)	(482,494,871)	(450,490,712)
Net change in total pension liability	(169,207,149)	228,815,372	598,423,523	783,711,199	498,847,261	465,309,653	1,083,334,062
Total pension liability - beginning	12,462,202,396	12,233,387,024	11,634,963,501	10,851,252,302	10,352,405,041	9,887,095,388	8,803,761,326
Total pension liability - ending	12,292,995,247	12,462,202,396	12,233,387,024	11,634,963,501	10,851,252,302	10,352,405,041	9,887,095,388
Plan fiduciary net position							
Contributions - employer	131,681,949	127,572,348	124,734,270	121,907,646	114,090,075	109,549,977	104,952,985
Contributions - member	131,541,783	127,454,956	124,262,387	122,144,961	114,443,295	110,152,580	106,175,381
Net investment income	192,238,245	583,573,718	911,695,475	1,431,977,414	22,836,265	435,682,659	1,695,543,796
Benefit payments, including refunds	(625,796,378)	(596,424,723)	(564,141,147)	(541,090,032)	(510,496,482)	(482,494,871)	(450,490,712)
Administrative expense	(5,127,029)	(5,095,897)	(4,870,334)	(4,363,512)	(3,944,641)	(3,911,222)	(3,853,073)
Cement plant consolidation	-	-	-	-	-	-	69,519,407
Net change in plan fiduciary net position	(175,461,430)	237,080,402	591,680,651	1,130,576,477	(263,071,488)	168,979,123	1,521,847,784
Plan fiduciary net position - beginning	12,472,799,657	12,235,719,255	11,644,038,604	10,513,462,127	10,776,533,615	10,607,554,492	9,085,706,708
Plan fiduciary net position - ending	\$ 12,297,338,227	\$ 12,472,799,657	\$ 12,235,719,255	\$ 11,644,038,604	\$ 10,513,462,127	\$ 10,776,533,615	\$ 10,607,554,492
System's net pension liability(asset) - ending	\$ (4,342,980)	\$ (10,597,261)	\$ (2,332,231)	\$ (9,075,103)	\$ 337,790,175	\$ (424,128,574)	\$ (720,459,104)

This schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, pension plans should present information for those years in which information is available.

See Notes to Schedules of Required Supplementary Information

SOUTH DAKOTA RETIREMENT SYSTEM

Schedule of Required Supplementary Information

June 30, 2020

	2020	2019	2018	2017	2016	2015	2014
SCHEDULE OF SYSTEM'S NET PENSION LIABILITY (ASSET)							
Total pension liability	\$ 12,292,995,247	\$ 12,462,202,396	\$ 12,233,387,024	\$ 11,634,963,501	\$ 10,851,252,302	\$ 10,352,405,041	\$ 9,887,095,388
Plan fiduciary net position	12,297,338,227	12,472,799,657	12,235,719,255	11,644,038,604	10,513,462,127	10,776,533,615	10,607,554,492
System's net pension liability (asset)	<u>\$ (4,342,980)</u>	<u>\$ (10,597,261)</u>	<u>\$ (2,332,231)</u>	<u>\$ (9,075,103)</u>	<u>\$ 337,790,175</u>	<u>\$ (424,128,574)</u>	<u>\$ (720,459,104)</u>
Plan fiduciary net position as a percentage of the							
Total pension liability	100.04%	100.09%	100.02%	100.08%	96.89%	104.10%	107.29%
Actuarial projected covered payroll	\$ 2,115,630,733	\$ 2,048,204,895	\$ 2,001,885,527	\$ 1,954,735,217	\$ 1,829,641,009	\$ 1,758,315,755	\$ 1,685,627,785
System's net pension liability (asset) as a percentage of covered payroll	-0.205%	-0.517%	-0.117%	-0.464%	18.462%	-24.121%	-42.741%

This schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, pension plans should present information for those years in which information is available.

SCHEDULE OF SYSTEM'S CONTRIBUTIONS

Last Fiscal Year

	2020	2019	2018	2017	2016	2015	2014
Actuarially determined contribution	\$ 131,681,949	\$ 127,572,348	\$ 124,734,270	\$ 121,907,646	\$ 114,090,075	\$ 109,549,977	\$ 103,483,647
Contributions in relation to the actuarially determined contribution	131,681,949	127,572,348	124,734,270	121,907,646	114,090,075	109,549,977	104,952,985
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (1,469,338)</u>
Reported covered payroll	\$ 2,115,630,733	\$ 2,048,204,895	\$ 2,001,885,527	\$ 1,954,735,217	\$ 1,829,641,009	\$ 1,758,315,755	\$ 1,685,627,785
Contributions as a percentage of covered payroll	6.224%	6.228%	6.231%	6.237%	6.236%	6.230%	6.226%

This schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, pension plans should present information for those years in which information is available.

See Notes to Required Supplementary Information

SOUTH DAKOTA RETIREMENT SYSTEM

Schedule of Required Supplementary Information

June 30, 2020

SCHEDULE OF INVESTMENT RETURNS

Last Fiscal Year

	<u>2020</u>	<u>2019</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>
Annual money-weighted rate of return, net of investment expenses	1.56%	4.84%	7.95%	13.84%	0.21%	4.17%	18.91%	19.01%	1.37%	25.27%
Annual time-weighted rate of return, net of investment expenses	1.59%	4.88%	7.94%	13.81%	0.30%	4.18%	18.90%	19.02%	1.45%	25.18%

See Notes to Required Supplementary Information

SOUTH DAKOTA RETIREMENT SYSTEM

Notes to Schedules of Required Supplementary Information

June 30, 2020

Methods and assumptions used in calculations of actuarially determined contributions. The actuarially determined contribution rates in the schedule of System's contributions are calculated as of July 1, two years prior to the end of the fiscal year in which contributions are reported. The following actuarial methods and assumptions were used to determine contribution rates reported in that schedule:

Valuation date	June 30, 2020
Amortization method	Level percentage of pay
Actuarial cost method	Entry age normal
Remaining amortization period	0 Years
Asset valuation method	Effective with the June 30, 2017 valuation, the actuarial value of assets is equal to the fair value of assets.
Actuarial assumptions:	
Investment rate of return	6.50%
Projected salary increases	6.50% at entry to 3.00% after 25 years of service
Post-retirement mortality table:	
Active Members	97% of RP-2014, adjusted to 2006 and projected generationally with Scale MP-2016, white collar rates for females and total dataset rates for males
Healthy inactive members, retired members and beneficiaries:	97% of RP-2014, adjusted to 2006 and projected generationally with Scale MP-2016, white collar rates for females and total dataset rates for males
Disabled inactive and retired members:	RP-2014 Disabled Mortality Table, adjusted to 2006 and projected generationally with Scale MP-2016



Other Supplementary Information
June 30, 2020

South Dakota Retirement System

SOUTH DAKOTA RETIREMENT SYSTEM

Other Supplementary Information

Year Ended June 30, 2020

Schedule of Administrative Expenses

Personal services:	
Salary and per diem	\$ 2,133,091
Employee benefits	<u>657,335</u>
Total personal services	<u>2,790,426</u>
Operating expenses:	
Travel	<u>60,992</u>
Contractual services:	
Audit	129,240
Finance	93,451
Valuations	65,000
Legal	249,185
Communications	59,561
Operations	<u>1,074,115</u>
Total contractual services	<u>1,670,552</u>
Supplies and materials	322,348
Capital assets	<u>282,711</u>
Total operating expenses	<u>2,336,603</u>
Total administrative expenses	<u><u>\$ 5,127,029</u></u>

SOUTH DAKOTA RETIREMENT SYSTEM

Other Supplementary Information

Year Ended June 30, 2020

Schedule of Investment Activity Expenses

Investment managers	
State of South Dakota Investment Council	\$ 9,366,489
Blackstone Private Equity	2,274,510
Blackstone Real Estate Partners	5,993,209
Brandes Global Mid-Cap	110,708
Brookfield Real Estate	1,555,872
Capital International	374,147
Carlyle	788,251
Cinven	6,709,622
CVC	2,125,613
Doughty Hanson & Co European Real Estate	61,587
Elevation Partners	4,807
Encap Energy	568,550
Lone Star Real Estate	2,922,957
Pinebridge	53,169
Riverstone	3,773,370
Rockpoint Real Estate	2,986,210
Sanders Capital	452,291
Silver Lake Partners LP	4,362,246
Starwood Real Estate	1,766,130
TCW Opp MBS Strategy	4,146,659
	<hr/>
Total investment activity expenses	\$ 50,396,397



Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of Trustees
South Dakota Retirement System
Pierre, South Dakota

We have audited, in accordance with the 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, the financial statements of the South Dakota Retirement System (SDRS), as of and for the year ended June 30, 2020, and the related notes to the financial statements, and have issued our report thereon dated November 4, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered SDRS's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of SDRS's internal control. Accordingly, we do not express an opinion on the effectiveness of the SDRS's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether SDRS's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "Eide Bailly LLP".

Boise, Idaho
November 4, 2020



Financial Statements
June 30, 2020

**South Dakota Retirement System
Supplemental Retirement Plan**



Independent Auditor's Report

To the Board of Trustees
South Dakota Retirement System
Pierre, South Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the South Dakota Retirement System Supplemental Retirement Plan (the Plan), which comprise the statement of fiduciary net position as of June 30, 2020, and the related statement of changes in fiduciary net position, for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective statement of fiduciary net position of the South Dakota Retirement System Supplemental Retirement Plan, as of June 30, 2020, and the respective statement of changes in fiduciary net position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 42-45 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 4, 2020, on our consideration of the Plan's 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 solely 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 effectiveness of the Plan's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Plan's internal control over financial reporting and compliance.



Boise, Idaho
November 4, 2020

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Management's Discussion and Analysis

June 30, 2020

This section presents management's discussion and analysis of the South Dakota Retirement System Supplemental Retirement Plan's (SRP or the Plan) financial position and performance for the year ended June 30, 2020. This section is intended to supplement the SRP financial statements.

Financial Highlights

- * The net position available for plan benefits of the SRP increased by \$37 million during fiscal year 2020. This increase was primarily attributable to investment gains during the year and contributions outweighing distributions to participants.
- * The SRP paid \$17.9 million to benefit recipients in fiscal year 2020 compared to \$17.7 million in 2019. The SRP received \$37.4 million in contributions in fiscal year 2020 compared to \$31.3 million in 2019.

Overview of the Financial Statements and Accompanying Information

The basic financial statements consist of:

Financial Statements

The Plan presents the statement of fiduciary net position as of June 30, 2020, and the statement of changes in fiduciary net position for the year then ended. These statements reflect resources available for the payment of benefits as of year-end and sources and uses of those funds during the year.

Notes to Financial Statements

The notes to financial statements are an integral part of the financial statements and provide additional detailed information and schedules.

Financial Analysis

The SRP was established in accordance with Internal Revenue Code Section 457 and under the administrative responsibility of the South Dakota Retirement System Board of Trustees. The Plan is funded by participant contributions and investment income. Marketing and record-keeping services for the Plan are provided by Nationwide Retirement Solutions, Inc.

SRP benefits are based on the participant balances in the Plan.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Management's Discussion and Analysis

June 30, 2020

A summary of the net position held in trust for plan benefits is shown below:

Summary of Fiduciary Net Position

June 30, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Assets		
Investments, at fair value	\$ 447,989,450	\$ 412,808,395
Cash	819,044	160,144
Accounts receivable	349,688	356,533
Accrued interest	2,002	2,048
Contributions receivable	<u>1,699,224</u>	<u>536,450</u>
Total assets	450,859,408	413,863,570
Liabilities		
Accounts payable	<u>67,507</u>	<u>38,580</u>
Net position held in trust for plan benefits	<u><u>\$ 450,791,901</u></u>	<u><u>\$ 413,824,990</u></u>

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Management's Discussion and Analysis

June 30, 2020

Change in Fiduciary Net Position

Additions to the net position include contributions and net investment income. Deductions from net position are primarily benefit payments. During 2020, SRP paid \$17.9 million to benefit recipients, or 1.02 percent more than 2019.

A summary of the changes in fiduciary net position is shown below:

Summary of Changes in Fiduciary Net Position

June 30, 2020 and 2019

	2020	2019	Percentage Change
Additions			
Contributions-employee	\$ 37,386,465	\$ 31,331,349	19.33%
Investment income	18,083,910	22,449,955	-19.45%
Other income (loss)	(6,845)	12,425	-155.09%
Transfers from related plan	227,552	653,485	-65.18%
Total additions	55,691,082	54,447,214	2.28%
Deductions			
Distributions to participants	17,930,344	17,748,612	1.02%
Administrative expenses	793,827	715,551	10.94%
Transfers to related plan	-	2,526	-100.00%
Total deductions	18,724,171	18,466,689	1.39%
Net change in net position	36,966,911	35,980,525	2.74%
Plan net position held in trust for plan benefits:			
Beginning of year	413,824,990	377,844,465	9.52%
End of year	\$ 450,791,901	\$ 413,824,990	8.93%

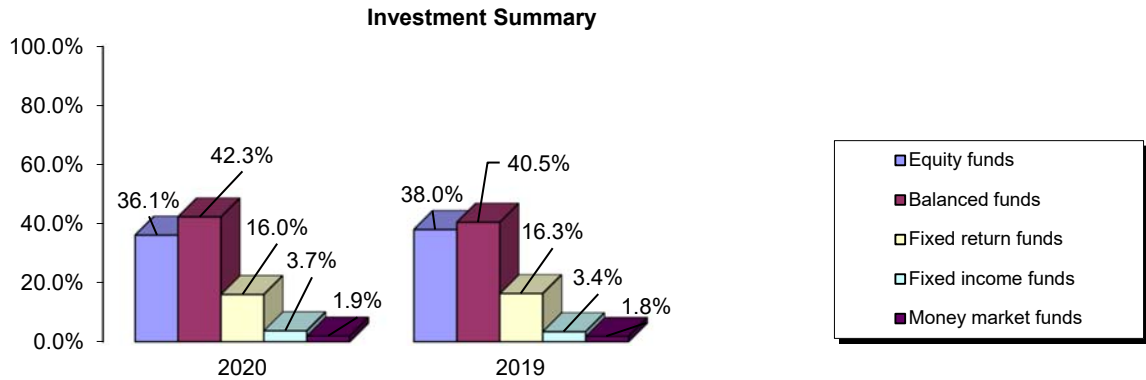
SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Management's Discussion and Analysis

June 30, 2020

Investments

The selection of SRP investment portfolio alternatives is the statutory responsibility of the South Dakota Investment Officer. The following exhibit indicates the percentage of investment in each of the SRP fund types.



Requests for Information

Requests for information about the SRP may be directed to the Supplemental Retirement Plan at 222 East Capitol Ave, Suite 1, Pierre SD 57501. You may reach the SRP at (605) 224-2230, 1 (800) 959-4457, or online at www.srp457.com. You may link to the SRP Web site from the SDRS Web site at www.state.sd.us/sdrs/.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Statement of Fiduciary Net Position

June 30, 2020

Assets

Investments, at fair value:

Equity funds	\$ 161,751,446
Balanced funds	189,214,531
Fixed return funds	71,888,920
Fixed income funds	16,600,217
Money market funds	<u>8,534,336</u>

Total investments, at fair value 447,989,450

Cash 819,044

Accounts receivable 349,688

Accrued interest 2,002

Contributions receivable 1,699,224

Total assets 450,859,408

Liabilities

Accounts payable 67,507

Net position held in trust for plan benefits \$ 450,791,901

See accompanying notes to financial statements.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Statement of Changes in Fiduciary Net Position

Year Ended June 30, 2020

Additions	
Contributions-employee	\$ 37,386,465
Investment income	18,083,910
Other income	(6,845)
Transfers from related plan	<u>227,552</u>
Total additions	<u>55,691,082</u>
Deductions	
Distributions to participants	17,930,344
Administrative expenses	<u>793,827</u>
Total deductions	<u>18,724,171</u>
Net change in plan net position	36,966,911
Net position held in trust for plan benefits	
Beginning of year	<u>413,824,990</u>
End of year	<u>\$ 450,791,901</u>

See accompanying notes to financial statements.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Notes to Financial Statements

June 30, 2020

(1) Plan Description

The following description of the South Dakota Retirement System Supplemental Retirement Plan (the Plan) provides only general information. Participants should refer to the plan provisions for a more complete description of the Plan.

(a) *General*

The Plan was established in July 1987 in accordance with Internal Revenue Code Section 457 under the administrative responsibility of the South Dakota Retirement System Board of Trustees. The state of South Dakota is a participating unit and every political subdivision thereof may become a participating unit in the Plan. The Plan consists of 25,606 participants and 346 employers. The Plan permits employees of participating units to defer a portion of their salary until future years. The deferred compensation is not available to the participants until termination, retirement, death, or unforeseeable emergency.

All amounts of compensation deferred under the Plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights held by the fund, at all times until made available to a participant or the participant's beneficiary, shall be held in trust for the exclusive benefit of the participant.

(b) *Contributions*

Participants of the Plan may contribute an amount of not less than \$25 per month and not in excess of \$19,500 for calendar year 2020 or 100 percent of includable compensation. A participant may make a one-time election to defer an additional amount of twice the otherwise applicable limit during any of the three calendar years immediately preceding a participant's elected normal retirement age. If age 50 or over, participants may also defer additional contributions of \$6,000.

There is a special catch-up provision that allows a participant for three years prior to the normal retirement age to contribute the lesser of:

- Twice the annual limit (\$39,000 in 2020) or
- The basic annual limit plus the amount of the basic limit not used in prior years (only allowed if not using age 50 or over catch-up contributions)

(c) *Participant's Account*

Each participant's account is credited with the participant's contributions, an allocation of the investment earnings or losses, and administrative expenses. Allocations are made based on the participant's percentage of the total investment balance. The benefit to which a participant is entitled is the benefit that can be provided from the participant's account.

(d) *Distribution to Participants*

Distributions of benefits to participants can be made upon termination, retirement, death, or unforeseeable emergency. Distributions are in the form of a lump-sum payment in cash equal to the value of the funds allocated to their account or installments, as defined in the plan agreement.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Notes to Financial Statements

June 30, 2020

(e) Vesting

Participants are vested immediately in their contributions plus actual earnings thereon.

(2) Summary of Significant Accounting Policies

(a) Basis of Accounting

The accompanying financial statements are prepared using the accrual basis of accounting. Revenue is recorded when earned and expenses recorded when incurred. Employee contributions are recognized when due pursuant to formal commitment, as well as statutory requirements. Distributions to participants are recognized when paid in accordance with the terms of the Plan.

(b) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires the plan administrator to make estimates and assumptions that affect the reported amounts of assets and liabilities, and changes therein, and disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

(3) Investments

Investments are reported at fair value, in accordance with GASB Statement No. 72. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GASB 72 sets forth the framework for measuring value. The framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels. The three levels of the fair value hierarchy under GASB 72 are described as follows:

Level 1 – Valuation inputs are quoted prices in active markets for identical asset or liability as of the measurement date.

Level 2 – Valuation inputs other than quoted prices included within Level 1 that are observable for an asset or liability, either directly or indirectly.

Level 3 – Valuation inputs are based on significant unobservable inputs for an asset or liability.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Notes to Financial Statements

June 30, 2020

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mutual funds	\$ 359,500,313	\$ 359,500,313	\$ -	\$ -
Fixed income funds	88,489,137	16,600,217	-	71,888,920
Investments at fair value	\$ 447,989,450	\$ 376,100,530	\$ -	\$ 71,888,920

Fair value for the mutual funds is determined based on the value of the underlying assets in the portfolio. Fixed return funds are carried at contract value, which approximates fair value.

Money market funds invest in short-term, interest-bearing instruments consisting of Treasury Bills, certificates of deposit, and commercial paper. Fixed income funds invest in interest-bearing instruments with varying maturities, including government or corporate bonds, notes, bills, and debentures. Equity funds invest in common and preferred stock and convertible securities of United States and foreign corporations. Balanced funds are invested in a combination of short-term, fixed income, and equity instruments. Fixed return funds are invested in an insurance company group annuity.

The interest rate on fixed return funds is set each quarter and guaranteed for up to two years. These funds are subject to certain restrictions. No more than 20 percent of the beginning of the year aggregate fixed return fund balance may be transferred annually to another investment alternative.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

Investments denominated in foreign currencies are translated into USD using the year-end spot foreign currency exchange rates. Foreign exchange rate gains and losses are included with the net appreciation in fair value of investments.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Notes to Financial Statements

June 30, 2020

Changes in fiduciary net position for the year ended June 30, 2020 by investment alternatives available to participants were as follows:

	Beginning balance	Contributions	Investment Income	Transfers In/Out	Additions/ Deductions	Ending balance	Fair value as a percentage of plan assets
Money Market							
Vanguard Treasury Money Market	\$ 630	\$ 2,646	\$ 23	\$ -	\$ (2,779)	\$ 520	0.00%
Vanguard Prime Money Market	-	(88)	-	-	88	-	0.00%
Vanguard Federal Money Market	7,600,465	1,140,263	116,170	-	(323,082)	8,533,816	1.89%
	7,601,095	1,142,821	116,193	-	(325,773)	8,534,336	1.89%
Fixed Return:							
Prudential	67,292,986	2,807,674	2,046,060	70,684	(328,484)	71,888,920	15.95%
Fixed Income							
Vanguard Bond Market	14,014,913	538,565	1,302,753	-	743,986	16,600,217	3.68%
Balanced							
* Vanguard InstTrgtRtrmInc Inst	9,475,755	56,709	531,471	-	(754,322)	9,309,613	2.07%
* Vanguard InstTrgRtrm2015 Inst	17,687,781	496,162	979,077	1,346	(704,812)	18,459,554	4.09%
* Vanguard InstTrgRtrm2020 Inst	34,692,305	2,399,394	1,639,658	23,872	(3,738,070)	35,017,159	7.77%
* Vanguard InstTrgRtrm2025 Inst	31,270,684	4,651,327	1,645,481	-	(671,353)	36,896,139	8.18%
* Vanguard InstTrgRtrm2030 Inst	21,903,104	4,918,498	1,079,767	-	(957,751)	26,943,618	5.98%
* Vanguard InstTrgRtrm2035 Inst	13,235,247	2,850,940	554,534	-	(981,058)	15,659,663	3.47%
* Vanguard InstTrgRtrm2040 Inst	10,693,331	1,884,421	407,442	-	(505,716)	12,479,478	2.77%
* Vanguard InstTrgRtrm2045 Inst	10,933,275	2,099,532	399,343	-	(298,842)	13,133,308	2.91%
* Vanguard InstTrgRtrm2050 Inst	10,569,833	2,037,471	363,610	-	(308,597)	12,662,317	2.81%
* Vanguard InstTrgRtrm2055 Inst	5,188,982	1,531,619	191,449	-	(338,015)	6,574,035	1.46%
* Vanguard InstTrgRtrm2060 Inst	1,362,930	530,472	52,046	-	(36,628)	1,908,820	0.42%
* Vanguard InstTrgRtrm2065 Inst	62,147	75,452	2,684	-	30,544	170,827	0.04%
* Vanguard InstTrgRtrm2035 Inv	-	88	268	-	(356)	-	0.00%
* Vanguard InstTrgRtrm2040 Inv	-	1,635	20	-	(1,655)	-	0.00%
* Vanguard InstTrgRtrm2050 Inv	-	-	225	-	(225)	-	0.00%
* Vanguard InstTrgRtrm2055 Inv	-	1,175	336	-	(1,511)	-	0.00%
* Vanguard InstTrgRtrm2060 Inv	-	-	335	-	(335)	-	0.00%
Total Balanced	167,075,374	23,534,895	7,847,746	25,218	(9,268,702)	189,214,531	41.97%
Equity							
* Franklin Mutual Shares	-	13	(1)	-	(12)	-	0.00%
* Vanguard Growth Indx Adml	306,369	238,233	374,132	-	1,706,219	2,624,953	0.58%
* Vanguard Value Indx Adml	180,899	99,966	57,698	-	659,236	997,799	0.22%
* Windsor II Admiral	29,680,907	635,883	45,071	-	(2,425,117)	27,936,744	6.20%
* Vanguard Instit Index	56,567,133	1,931,466	4,262,858	24,937	(4,434,245)	58,352,149	12.94%
* Vanguard Tot Intl Stock Ind	9,226,951	436,984	(267,327)	24,804	(1,221,808)	8,199,604	1.82%
* Dodge Cox Global Stock	1,201,932	373,351	(25,859)	-	(16,034)	1,533,390	0.34%
* Dodge & Cox Int Stock Fnd	2,727,562	165,825	(299,780)	-	21,980	2,615,587	0.58%
* Growth Fund of America	14,794,188	1,001,198	2,426,251	12,433	(1,308,623)	16,925,447	3.75%
* Capital World Grth & Inc	6,090,684	445,575	162,198	-	(360,249)	6,338,208	1.41%
* Vanguard Small Cap Index Fd AS	4,286,027	493,245	(218,569)	48,017	(134,521)	4,474,199	0.99%
* Vanguard Ext Mkt Idx Inst	16,562,463	725,336	204,068	21,459	(1,546,750)	15,966,576	3.54%
* Vanguard Wsly Inc Adml	9,408,568	572,421	519,457	-	32,960	10,533,406	2.34%
* Vanguard Strategic Equity	5,790,344	423,388	(471,041)	-	(489,307)	5,253,384	1.17%
Total Equity	156,824,027	7,542,884	6,769,156	131,650	(9,516,271)	161,751,446	35.88%
Total Investments	412,808,395	35,566,839	18,081,908	227,552	(18,695,244)	447,989,450	99.38%
Other Net Assets	1,016,595	1,819,626	(4,843)	-	(28,927)	2,802,451	0.62%
Total plan assets	\$ 413,824,990	\$ 37,386,465	\$ 18,077,065	\$ 227,552	\$ (18,724,171)	\$ 450,791,901	100.00%

Investments in bold represent investments exceeding 5 percent or more of net position as of June 30, 2020. Investments with an asterisk (*) represent investments with international mutual funds.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Notes to Financial Statements

June 30, 2020

Risks and Uncertainties

The Plan invests in various investment securities. These securities are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the statement of fiduciary net position. Since all investments are participant directed, all risks exist at the participant level. Each individual within the plan has the responsibility for managing their exposure to fair value loss.

(a) Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The portfolios of the SDRS Supplemental Retirement Plan are benchmarked to the duration of the International Index and must fall between 70 percent and 130 percent of the duration.

As of June 30, 2020, the Plan had the following investments and maturities in its fixed income investment and certain mutual funds which include investments in bonds. The durations of the various investment types are listed in the following table:

Fixed Income	Fair Value	Ave Credit Quality	Ave Eff Maturity
Vanguard Total Bond Market Index	\$ 15,869,807	AA	8.40
Balanced			
Vanguard InstTrgtRtrmInc Inst	\$ 6,154,585	AA	7.21
Vanguard InstTrgRtrm2015 Inst	11,276,942	AA	7.31
Vanguard InstTrgRtrm2020 Inst	16,650,659	AA	7.68
Vanguard InstTrgRtrm2025 Inst	13,968,878	A	8.62
Vanguard InstTrgRtrm2030 Inst	8,188,166	A	8.65
Vanguard InstTrgRtrm2035 Inst	3,609,552	A	8.65
Vanguard InstTrgRtrm2040 Inst	1,976,749	A	8.65
Vanguard InstTrgRtrm2045 Inst	1,147,851	A	8.71
Vanguard InstTrgRtrm2050 Inst	1,120,615	A	8.70
Vanguard InstTrgRtrm2055 Inst	600,209	A	8.68
Vanguard InstTrgRtrm2060 Inst	174,084	A	8.65
Vanguard InstTrgRtrm2065 Inst	16,177	A	8.81
	<u>\$ 80,754,274</u>		

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Notes to Financial Statements

June 30, 2020

(b) Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. As of June 30, 2020, the portfolios held the following investments, excluding those issued by or explicitly guaranteed by the U.S. government, which are not considered to have credit risk. The investments are grouped as rated by Moody's Investors Service.

	<u>Fair Value</u>
Moody's rating:	
A	\$ 30,802,281
AA	49,951,993
Unrated	7,734,863
Total	<u>\$ 88,489,137</u>

(c) Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the plan's investment in a single issuer. The Plan's investments are managed by several fund managers. The concentration of investments are determined by the participants' elections to invest in available investments options as selected by the SD Investment Council. The investments that exceed 5 percent are identified in bold on page 51.

(d) Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates could adversely affect the fair value of the investment. The Plan allows the option of investments in mutual funds of countries outside the U.S. that invest in securities not required to disclose the individual assets within the fund. The fair value of these investments was \$67,137,024 as of June 30, 2020. International mutual funds are marked with asterisk on page 51.

(4) Plan Administration

Nationwide Retirement Solutions, Inc. (NRS) of Columbus, Ohio, is the private sector administrator and marketing agent of the Plan. NRS provides various accounting, reporting, and marketing services and receives compensation through maintenance and asset fees charged against each participant account.

(5) Federal Income Tax Status

The Plan is an eligible nonqualified deferred compensation plan under Section 457(a) of the Internal Revenue Code and is exempt from federal income taxes. The Plan has received a favorable determination letter dated September 15, 1988. The Plan has been amended since receiving the determination letter. However, the plan administrator and the Plan's tax counsel believe that the Plan is currently designed and being operated in compliance with the applicable requirements of the Internal Revenue Code. Therefore, no provision for income taxes has been included in the Plan's financial statements.

SOUTH DAKOTA RETIREMENT SYSTEM SUPPLEMENTAL RETIREMENT PLAN

Notes to Financial Statements

June 30, 2020

(6) Plan Termination

Although they have not expressed any intent to do so, the South Dakota Retirement System Board of Trustees and the South Dakota Legislature have the right to terminate the Plan. In the event of plan termination, participants continue to be 100 percent vested in their account balances.



Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of Trustees
South Dakota Retirement System
Pierre, South Dakota

We have audited, in accordance with the 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, the financial statements of the South Dakota Retirement System Supplemental Retirement Plan (SRP), as of and for the year ended June 30, 2020, and the related notes to the financial statements, and have issued our report thereon dated November 4, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered SRP's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of SRP's internal control. Accordingly, we do not express an opinion on the effectiveness of the SRP's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether SRP's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "Eide Sully LLP".

Boise, Idaho
November 4, 2020



Financial Statements
June 30, 2020

South Dakota Retirement System
Special Pay Plan



Independent Auditor's Report

To the Board of Trustees
South Dakota Retirement System
Pierre, South Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the South Dakota Retirement System Special Pay Plan (SPP or the Plan), which comprise the statement of fiduciary net position as of June 30, 2020, and the related statement of changes in fiduciary net position, for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective statement of fiduciary net position of the South Dakota Retirement System Special Pay Plan, as of June 30, 2020, and the respective statement of changes in fiduciary net position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 59-62 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 4, 2020, on our consideration of the Plan's 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 solely 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 effectiveness of the Plan's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Plan's internal control over financial reporting and compliance.

The image shows a handwritten signature in cursive script that reads "Eide Bailly LLP". The signature is written in dark ink and is positioned above the typed name and date.

Boise, Idaho
November 4, 2020

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Management's Discussion and Analysis

June 30, 2020

This section presents management's discussion and analysis of the South Dakota Retirement System Special Pay Plan's (SPP or the Plan) financial position and performance for the year ended June 30, 2020. This section is intended to supplement the SPP financial statements and notes.

Financial Highlights

- The net position available for plan benefits of the SPP increased by \$4.4 million during fiscal year 2020. This increase was primarily attributable to additional participant contributions and investment gains.
- The SPP paid \$8.3 million to benefit recipients in fiscal year 2020 compared to \$6.3 million in 2019. The SPP received \$11.0 million in contributions in fiscal year 2020 compared to \$10.1 million in 2019.

Overview of the Financial Statements and Accompanying Information

The basic financial statements consist of:

Financial Statements

The Plan presents the statement of fiduciary net position as of June 30, 2020, and the statement of changes in fiduciary net position for the year then ended. These statements reflect resources available for the payment of benefits as of year-end and sources and uses of those funds during the year.

Notes to Financial Statements

The notes to financial statements are an integral part of the financial statements and provide additional detailed information and schedules.

Financial Analysis

The SPP was established in accordance with Internal Revenue Code Section 401 and under the administrative responsibility of the South Dakota Retirement System Board of Trustees. The Plan is funded by participant contributions and investment income. Marketing and record-keeping services for the Plan are provided by Nationwide Retirement Solutions, Inc.

SPP benefits are based on the participant balances in the Plan.

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Management's Discussion and Analysis

June 30, 2020

A summary of the net position held in trust for plan benefits is shown below:

Summary of Fiduciary Net Position

June 30, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Assets		
Investments, at fair value	\$ 63,453,746	\$ 58,643,373
Cash	1,358,253	25,940
Revenue sharing receivable	59,213	54,588
Accrued interest	916	523
Contributions receivable	<u>397,102</u>	<u>2,156,631</u>
Total assets	65,269,230	60,881,055
Liabilities		
Accounts payable	<u>7,560</u>	<u>8,685</u>
Net position held in trust for plan benefits	<u><u>\$ 65,261,670</u></u>	<u><u>\$ 60,872,370</u></u>

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Management's Discussion and Analysis

June 30, 2020

Changes in Fiduciary Net Position

Additions to the net position mainly were due to contributions during the year. Deductions from net position are primarily benefit payments and administrative expenses. During 2020, SPP paid \$8.3 million to benefit recipients, or 31.37 percent more than 2019.

A summary of the changes in fiduciary net position is shown below:

Summary of Changes in Fiduciary Net Position

June 30, 2020 and 2019

	<u>2020</u>	<u>2019</u>	<u>Percentage Change</u>
Additions			
Contributions-employee	\$ 11,012,037	\$ 10,111,260	8.91%
Investment income	1,981,982	1,872,227	5.86%
Revenue sharing	4,625	-	100.00%
Other income	<u>34,155</u>	<u>34,650</u>	-1.43%
Total additions	<u>13,032,799</u>	<u>12,018,137</u>	8.44%
Transfers from related plan	<u>-</u>	<u>2,526</u>	-100.00%
Deductions			
Distributions to participants	8,291,154	6,311,180	31.37%
Administrative expenses	124,793	116,723	6.91%
Revenue sharing loss	<u>-</u>	<u>1,695</u>	-100.00%
Total deductions	<u>8,415,947</u>	<u>6,429,598</u>	30.89%
Transfers to related plans	227,552	653,485	
Net change in plan net position	<u>4,389,300</u>	<u>4,937,580</u>	-11.10%
Net position held in trust for plan benefits:			
Beginning of year	<u>60,872,370</u>	<u>55,934,790</u>	8.83%
End of year	<u>\$ 65,261,670</u>	<u>\$ 60,872,370</u>	7.21%

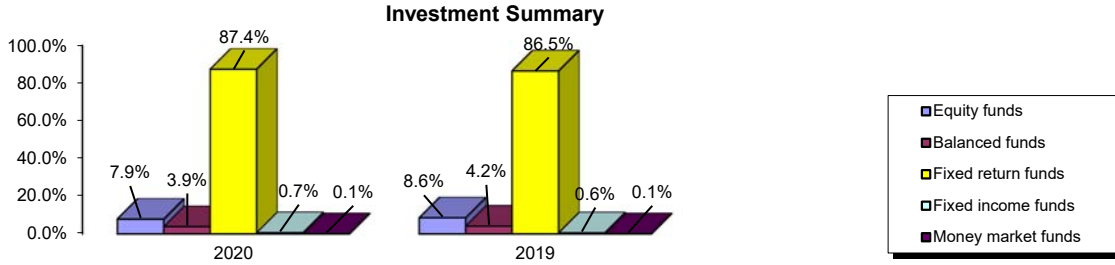
SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Management's Discussion and Analysis

June 30, 2020

Investments

The selection of SPP investment portfolios alternatives is the statutory responsibility of the South Dakota Investment Officer. The following exhibit indicates the percentage of investment in each of the SPP fund types.



Requests for Information

Requests for information about the SPP may be directed to the Special Pay Plan at 222 East Capitol Ave, Suite 1, Pierre SD 57501. You may reach the SPP at (605) 224-2230 or 1 (800) 959-4457.

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Statement of Fiduciary Net Position

June 30, 2020

Assets

Investments, at fair value:

Equity funds	\$ 5,019,448
Balanced funds	2,474,228
Fixed return funds	55,452,290
Fixed income funds	447,081
Money market funds	<u>60,699</u>

Total investments, at fair value 63,453,746

Cash 1,358,253

Revenue sharing receivable 59,213

Accrued interest 916

Contributions receivable 397,102

Total assets 65,269,230

Liabilities

Accounts payable 7,560

Net position held in trust for plan benefits \$ 65,261,670

See accompanying notes to financial statements.

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Statement of Changes in Fiduciary Net Position

Year Ended June 30, 2020

Additions	
Contributions-employee	\$ 11,012,037
Investment income	1,981,982
Revenue sharing	4,625
Other income	34,155
	<hr/>
Total additions	13,032,799
	<hr/>
Deductions	
Distributions to participants	8,291,154
Administrative expenses	124,793
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Total deductions	8,415,947
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Transfers from related plan	227,552
	<hr/>
Net change in plan net position	4,389,300
Net position held in trust for plan benefits:	
Beginning of year	60,872,370
	<hr/>
End of year	\$ 65,261,670
	<hr/> <hr/>

See accompanying notes to financial atatements.

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Notes to Financial Statements

June 30, 2020

(1) Plan Description

The following description of the South Dakota Retirement System Special Pay Plan (the Plan) provides only general information. Participants should refer to the plan provisions for a more complete description of the Plan.

(a) *General*

The Plan was established in July 2004 as a qualified plan pursuant to Internal Revenue Code Section 401(a) under the administrative responsibility of the South Dakota Retirement System Board of Trustees. South Dakota state government and the South Dakota Board of Regents are participating units and every state political subdivision may become a participating unit in the Plan. The Plan consists of 3,122 participants and 134 employers. The Plan mandates that qualifying employees (over age 55 and \$600 or more in special pay) of participating units defer 100 percent of their special lump-sum termination pay to the plan. Special pay is compensation other than regular salary or wages granted to a member of the South Dakota Retirement System and transferred in a sum to the Plan at termination of the member's employment. The participating unit transfers the deferred pay to the fund. This deferred pay is available to a participant immediately after termination, upon later retirement, or to beneficiaries or an estate upon the participant's death.

All amounts of special termination pay deferred under the Plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights held by the fund, at all times until made available to a participant or the participant's beneficiary for estate, shall be held in trust for the exclusive benefit of the participant.

(b) *Contributions*

Participants in the Plan can contribute the lesser of 100 percent of their one-time, lump-sum special pay associated with their termination or \$57,000 for calendar year 2020.

(c) *Participant's Account*

Each participant's account is credited with the participant's contribution, an allocation of the investment earnings or losses, and administrative expenses. Allocations are made based on the participant's percentage of the total investment balance. The benefit to which a participant is entitled is the benefit that can be provided from the participant's account.

(d) *Distribution to Participants*

Distributions of benefits to participants can be made immediately after the participant's termination, or upon the participant's retirement, or to a beneficiary or an estate upon the participant's death. Distributions are in the form of a lump-sum payment in cash equal to the value of the funds allocated to their account or in the form of installments as defined in the plan agreement.

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Notes to Financial Statements

June 30, 2020

(e) *Risks and Uncertainties*

The Plan invests in various investment securities. These securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the statement of fiduciary net position.

(2) Summary of Significant Accounting Policies

(a) *Basis of Accounting*

The accompanying financial statements are prepared using the accrual basis of accounting. Revenue is recorded when earned and expenses recorded when incurred. Employee contributions are recognized when due pursuant to formal commitment, as well as statutory requirements. Distributions to participants are recognized when paid in accordance with the terms of the Plan.

(b) *Use of Estimates*

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires the plan administrator to make estimates and assumptions that affect the reported amounts of assets and liabilities, and changes therein, and disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

(3) Investments

Investments are reported at fair value, in accordance with GASB Statement No. 72. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GASB 72 sets forth the framework for measuring value. The framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels. The three levels of the fair value hierarchy under GASB 72 are described as follows:

Level 1 – Valuation inputs are quoted prices in active markets for identical asset or liability as of the measurement date.

Level 2 – Valuation inputs other than quoted prices included within Level 1 that are observable for an asset or liability, either directly or indirectly.

Level 3 – Valuation inputs are based on significant unobservable inputs for an asset or liability.

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Notes to Financial Statements

June 30, 2020

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Mutual funds	\$ 8,001,456	\$ 8,001,456	\$ -	\$ -
Fixed income funds	55,452,290	-	-	55,452,290
Investments at fair value	\$ 63,453,746	\$ 8,001,456	\$ -	\$ 55,452,290

Fair value for the mutual funds is determined based on the value of the underlying assets in the portfolio. Fixed return funds are carried at contract value, which approximates fair value.

Money market funds invest in short-term, interest-bearing instruments consisting of Treasury Bills, certificates of deposit, and commercial paper. Fixed income funds invest in interest-bearing instruments with varying maturities, including government or corporate bonds, notes, bills, and debentures. Equity funds invest in common and preferred stock and convertible securities of United States and foreign corporations. Balanced funds are invested in a combination of short-term, fixed income, and equity instruments. Fixed return funds are invested in an insurance company group annuity.

The interest rate on fixed return funds is set each quarter and guaranteed for up to two years. These funds are subject to certain restrictions. No more than 20 percent of the beginning of the year aggregate fixed return fund balance may be transferred annually to another investment alternative.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

Investments denominated in foreign currencies are translated into USD using the year-end spot foreign currency exchange rates. Foreign exchange rate gains and losses are included with the net appreciation in fair value of investments.

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Notes to Financial Statements

June 30, 2020

Changes in fiduciary net position for the year ended June 30, 2020 by investment alternatives available to participants were as follows:

	Beginning Balance	Contributions	Investment Income	Transfers In/Out	Additions/ Deductions	Ending Balance	Fair Value as a Percentage of Plan Assets
Money Market							
Vanguard Federal	\$ 52,814	\$ -	\$ 703	\$ -	\$ 7,182	\$ 60,699	0.09%
Fixed Return:							
Prudential	50,740,118	11,418,254	1,566,526	(153,939)	(8,118,669)	55,452,290	84.97%
Fixed Income							
Vanguard Bond Market	377,606	5,358	35,931	-	28,186	447,081	0.69%
Balanced							
Vngrd InstTrgtRtrmInc Inst	731,649	-	38,428	-	(190,195)	579,882	0.89%
Vngrd InstTrgRtrm2015 Inst	439,558	-	24,106	-	(37,974)	425,690	0.65%
Vngrd InstTrgRtrm2020 Inst	876,780	-	49,520	(23,872)	(551,804)	350,624	0.54%
Vngrd InstTrgRtrm2025 Inst	213,404	-	(896)	-	622,805	835,313	1.28%
Vngrd InstTrgRtrm2030 Inst	63,836	-	3,411	-	79,968	147,215	0.23%
Vngrd InstTrgRtrm2035 Inst	31,039	-	58	-	25,105	56,202	0.09%
Vngrd InstTrgRtrm2040 Inst	19,233	-	665	-	(22)	19,876	0.03%
Vngrd InstTrgRtrm2050 Inst	50,285	-	1,507	-	(1,625)	50,167	0.08%
Vngrd InstTrgRtrm2060 Inst	8,999	-	274	-	(14)	9,259	0.01%
Total Balanced	2,434,783	-	117,073	(23,872)	(53,756)	2,474,228	3.79%
Equity							
Dodge and Cox Int Stock Fd	49,567	-	(4,072)	-	8,765	54,260	0.08%
DodgeCox Global Stock	123,519	-	(9,692)	-	(8,106)	105,721	0.16%
Am Funds Capital World Grth &	140,333	-	1,946	-	(127)	142,152	0.22%
Vanguard Ext Mkt Ind Inst	728,220	-	860	-	(89,459)	639,621	0.98%
Growth Fund of America	974,507	7,001	120,585	-	(201,177)	900,916	1.38%
Mutual Shares	-	-	-	-	-	-	0.00%
Windsor II Admiral	437,785	-	1,738	-	(42,733)	396,790	0.61%
Vanguard Small Cap Indx Fd AS	324,336	-	(27,624)	-	(107,411)	189,301	0.29%
Vanguard Instit Index	1,302,210	8,038	88,754	(24,937)	(168,387)	1,205,678	1.85%
Vanguard Tot Intl Stock Ind	195,510	-	(5,876)	(24,804)	(34,287)	130,543	0.20%
Vanguard Wlsly Inc Adml	522,700	-	28,543	-	(56,583)	494,660	0.76%
Vanguard Gr Indx Adml	39,402	-	82,603	-	449,471	571,476	0.88%
Vanguard Val Indx Adml	3,885	-	(1,595)	-	16,781	19,071	0.03%
Vanguard Strategic Equity	196,078	-	(15,337)	-	(11,482)	169,259	0.26%
Total Equity	5,038,052	15,039	260,833	(49,741)	(244,735)	5,019,448	7.69%
Total Investments	58,643,373	11,438,651	1,981,066	(227,552)	(8,381,792)	63,453,746	97.23%
Other Assets	2,228,997	(426,614)	5,541	-	-	1,807,924	2.77%
Total Plan Net Assets	\$ 60,872,370	\$ 11,012,037	\$ 1,986,607	\$ (227,552)	\$ (8,381,792)	\$ 65,261,670	100.00%

Investments in bold represent investments exceeding 5 percent or more of net position as of June 30, 2020.

SOUTH DAKOTA RETIREMENT SYSTEM SPECIAL PAY PLAN

Notes to Financial Statements

June 30, 2020

(4) Plan Administration

Nationwide Retirement Solutions, Inc. (NRS) of Columbus, Ohio, is the private sector administrator and marketing agent of the Plan. NRS provides various accounting, reporting, and marketing services and receives compensation through maintenance and asset fees charged against each participant account.

(5) Federal Income Tax Status

The Plan is a qualified plan under Section 401(a) of the Internal Revenue Code and is exempt from federal income taxes. The Plan has received a favorable determination letter dated October 28, 2004. The Plan has been amended since receiving the determination letter. However, the plan administrator and the Plan's tax counsel believe that the Plan is currently designed and being operated in compliance with the applicable requirements of the Internal Revenue Code. Therefore, no provision for income taxes has been included in the Plan's financial statements.

(6) Plan Termination

Although they have not expressed any intent to do so, the South Dakota Retirement System Board of Trustees and the South Dakota Legislature have the right to terminate the Plan. In the event of plan termination, participants would continue to be 100 percent vested in their account balances.



Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of Trustees
South Dakota Retirement System
Pierre, South Dakota

We have audited, in accordance with the 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, the financial statements of the South Dakota Retirement System Special Pay Plan (SPP), as of and for the year ended June 30, 2020, and the related notes to the financial statements, and have issued our report thereon dated November 4, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered SPP's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of SPP's internal control. Accordingly, we do not express an opinion on the effectiveness of the SPP's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether SPP's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Eide Sully LLP". The signature is written in a cursive, flowing style.

Boise, Idaho
November 4, 2020