

SOUTH DAKOTA INVESTMENT COUNCIL

AUDIT REPORT

Fiscal Year Ended June 30, 2020



State of South Dakota
Department of Legislative Audit
427 South Chapelle
% 500 East Capitol
Pierre, SD 57501-5070

SOUTH DAKOTA INVESTMENT COUNCIL
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RUSSELL A. OLSON
AUDITOR GENERAL

**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**

Executive Board
Legislative Research Council

and

Investment Council
State of 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 Cash Flow portfolio, an internal investment pool of the State of South Dakota, as of and for the year ended June 30, 2020, and the related notes to the financial statements, which collectively comprise the Cash Flow portfolio's basic financial statements and have issued our report thereon dated October 2, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the South Dakota Investment Council'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 the South Dakota Investment Council's internal control. Accordingly, we do not express an opinion on the effectiveness of the South Dakota Investment Council'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 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 the South Dakota Investment Council's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, 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. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.

A handwritten signature in black ink that reads "Russell A. Olson". The signature is written in a cursive, flowing style.

Russell A. Olson
Auditor General

October 2, 2020



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RUSSELL A. OLSON
AUDITOR GENERAL

INDEPENDENT AUDITOR'S REPORT

Executive Board
Legislative Research Council

and

Investment Council
State of South Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the Cash Flow portfolio, an internal investment pool of the State of South Dakota, as of and for the fiscal year ended June 30, 2020, and related notes to the financial statements, as listed in the table of contents.

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 financial position of the portfolio listed above as of June 30, 2020, and the changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

The financial statements present only the above referenced investment portfolio managed by the South Dakota Investment Council and do not purport to, and do not, present fairly the financial position of the State of South Dakota as of June 30, 2020, the changes in its financial position, or, where applicable, its cash flows for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 2, 2020, on our consideration of the South Dakota Investment Council's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, 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 South Dakota Investment Council'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 South Dakota Investment Council's internal control over financial reporting and compliance.



Russell A. Olson
Auditor General

October 2, 2020

South Dakota Investment Council
Cash Flow Portfolio
Statement of Net Position
As of June 30, 2020

Assets	
Cash & cash equivalents	\$ 28,027,865
Investment income receivable	7,497,351
Investments, at fair value	
Short term investment fund	1,428,192,591
Fixed income	1,244,726,258
Total investments	2,672,918,849
Total assets	2,708,444,065
Liabilities	
Earnings distribution - declared	37,624,155
Total liabilities	37,624,155
Net Position	\$ 2,670,819,910

The accompanying notes are an integral part of the financial statements.

South Dakota Investment Council
Cash Flow Portfolio
Statement of Changes in Net Position
For the fiscal year ended June 30, 2020

Additions:	
Contributions	\$ 1,327,448,561
Investment income (loss):	
<i>From investing activities:</i>	
Net appreciation in fair value of investments	43,773,292
Interest	32,510,264
Investment income	76,283,556
Less investment activity expense	(507,355)
<i>Net investment activity income</i>	75,776,201
Total investment income	75,776,201
Total additions	1,403,224,762
Deductions:	
Statutorily required distributions	37,624,155
Total deductions	37,624,155
Net increase in net position	1,365,600,607
Net position - Beginning of year	1,305,219,303
Net position - End of year	\$ 2,670,819,910

The accompanying notes are an integral part of the financial statements.

SOUTH DAKOTA INVESTMENT COUNCIL
CASH FLOW PORTFOLIO
NOTES TO THE FINANCIAL STATEMENTS

1. Reporting Entity:

The South Dakota Investment Council (SDIC) is a principal, functional sub-unit of state government. The SDIC is responsible for the investment of the state's monies in the state treasury. The SDIC provides investment management services on a prefunded cost recovery basis as authorized by South Dakota Codified Law (SDCL) 4-5-30.

The statements represent the financial activity of the Cash Flow portfolio. The Cash Flow portfolio represents the state's aggregate idle fund monies for all state funds, except certain funds for which separate portfolios have been established.

2. Summary of Significant Accounting Policies:

a. Basis of Presentation:

The accompanying financial statements of the investment activity of the SDIC on behalf of the Cash Flow portfolio are prepared in accordance with generally accepted accounting principles (GAAP) for governments as prescribed by the Governmental Accounting Standards Board (GASB).

b. Basis of Accounting:

The statements for the portfolio are reported on the full accrual basis of accounting. Under this method, revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred. Security transactions and the related gains and losses are recorded on a trade date basis using the average cost method. Interest income is accrued as earned.

c. Cash and Cash Equivalents:

Cash includes demand deposits. Cash equivalents include non-negotiable certificates of deposit, which are reported at cost.

d. Valuation of Securities:

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.

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 or securities 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 4: Fair Value Measurement.

e. Use of Estimates:

The preparation of financial statements in accordance with GAAP requires management to make estimates that affect the reported amounts of net position as of June 30, 2020. Actual results could differ from those estimates.

f. New GAAP Implementation:

Government Accounting Standards Board did not issue any new or updated statements that affected SDIC for fiscal year 2020.

3. Deposits, Investments and Securities Lending:

The State Investment Officer is responsible for the investment of state public funds. State public funds in the Cash Flow portfolio are invested using the pooled deposit and investment concept which preserves the integrity of the fund cash balances of each state fund while simultaneously allowing the deposit and investment of aggregate idle fund monies. The Cash Flow portfolio may be invested in the following classes of securities and investments and not otherwise:

- (1) Direct and indirect obligations of the United States government;
- (2) Agencies and instrumentalities of the United States government;
- (3) Direct obligations of the State of South Dakota and any of its political subdivisions;
- (4) Obligations consisting of notes, bonds, debentures, and certificates which are direct obligations of a solvent corporation or trust existing under the laws of the United States or any state thereof, if such investments are rated in the four highest classifications established by at least two standard rating services at the time of purchase;
- (5) Savings accounts, share accounts, certificates of deposit of banks, savings and loan associations, building and loan associations and bankers' acceptances;
- (6) In addition to the investments authorized by subdivisions (1) to (5) of this section, inclusive, the investment council may also allocate a sum certain of state public funds for investment in the accounts and certificates of South Dakota banks and associations. This sum shall initially be offered to South Dakota banks and associations, and if not initially fully subscribed, the investment officer shall immediately reoffer the unsubscribed sum to other qualified public depositories. "Qualified public depository" is a state bank and loan association or federally chartered credit union located in this state which receives or holds public deposits and segregates eligible collateral for public deposits.

Deposits:

Custodial Credit Risk. 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 in the possession of an outside party. The Cash Flow portfolio's certificates of deposit and other deposits in state financial institutions in excess of depository insurance must be 100% collateralized. Collateral is valued at the lower of cost or market as reported in the quarterly call reports prepared by the qualified public depositories pursuant to SDCL 4-6A-7. Collateral is required to be segregated by each depository as approved by the South Dakota Public Deposit Protection Commission. Collateral may not be held in any safety deposit vault owned or controlled either directly or indirectly by the pledging financial institution, but must be deposited for safekeeping in a financial institution that is a member of the Federal Reserve. As of June 30, 2020, pledged collateral for one depository did not equal at least 100 percent of the total public deposits in excess of depository insurance. As a result, \$90,436 of the Cash Flow portfolio's certificates of deposit was exposed to custodial credit risk.

Investments:

Securities Lending. State statutes and the SDIC policies permit the use of investments for securities lending transactions. These transactions involve the lending of corporate debt 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. The SDIC'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% of fair value plus accrued interest for corporate debt securities. The earnings generated from the collateral investments results in the gross earnings from lending activities, which is then split on a percentage basis with the lending agent.

The Cash Flow portfolio did not have any securities on loan as of June 30, 2020 so the portfolio did not have any credit risk exposure to borrowers.

The contract with the lending agent requires the agent to indemnify the SDIC 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 the SDIC or the borrower. The SDIC does not have the ability to pledge or sell collateral securities unless the borrower defaults. 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.

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. The SDIC's securities lending policies are detailed in the preceding Securities Lending section. As of June 30, 2020, the Cash Flow portfolio does not have custodial credit risk with regard to securities lending.

Interest Rate Risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. SDIC policy limits or establishes ranges for the durations of the fixed income portfolios. Modified duration estimates the sensitivity of a bond's price to interest rate changes. The Cash Flow short term portfolio policy limits average portfolio duration to 2.88 years, and no holding's maturity can exceed 5.25 years. The Cash Flow intermediate term portfolio is benchmarked to the duration of the FTSE Broad Investment Grade (BIG) Index. The fair value (in USD) and weighted modified duration (in years) of the Cash Flow portfolio as of June 30, 2020 is listed in the following table:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Weighted Modified Duration</u>
U.S. Treasuries	\$ 16,096,950	3.43
U.S. Treasury STRIPS	113,005,441	9.29
U.S. Agencies	332,188,310	2.78
Investment Grade Corporates	677,038,061	2.46
High Yield Corporates	9,802,661	1.81
Agency Mortgage-Backed Securities	<u>96,594,835</u>	2.55
TOTAL	<u>\$ 1,244,726,258</u>	
Portfolio modified duration		3.18

The Cash Flow portfolio invests in mortgage-backed securities. These securities are sensitive to prepayments by mortgagees, which is likely in declining interest rate environments, which can reduce the value of these securities.

Credit Risk. Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. SDIC guidelines establish a percentage range and a normal allocation to various credit risk categories. The Cash Flow short-term portfolio can invest 4% of the portfolio into each corporate security rated Aaa or Aa, 3% in A-rated, 1% in Baa1 or Baa2, and 0.5% in Baa3-rated individual holdings of corporate securities. Credit rating limits are 15% of the total short-term portfolio or up to 20% with the Investment Officer's permission for Baa-rated and 5% of the total portfolio or up to 10% with the Investment Officer's permission on downgraded securities below Baa. The SDIC reviews the investment guidelines annually for the Cash Flow intermediate-term portfolio. These guidelines establish the benchmark percentage invested in each fixed income asset category and the minimum and maximum range of each fixed income asset category. As of June 30, 2020, the total portfolio 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 (at fair value):

Moody's rating:	
Aaa	\$ 1,778,264,409
Aa	128,502,043
A	440,974,384
Baa	89,678,126
Ba	9,802,661
Total	<u>\$ 2,447,221,623</u>

Concentration of Credit Risk. Concentration of credit risk is the risk of loss that may be attributed to the magnitude of a government's investment in a single issuer. The Cash Flow portfolio has a policy in place limiting its investments in individual holdings. Information regarding the policy is located in the Credit Risk section. Additionally, there are no single issuer exposures (excluding those issued by or explicitly guaranteed by the U.S. Government, or involving mutual funds or investment pools) within the portfolio that comprises 5% of the overall portfolio as of June 30, 2020.

4. Fair Value Measurement:

Investments are reported at fair value as of June 30, 2020, to the extent available. GASB Statement No. 72 – *Fair Value Measurement and Application*, defines fair value as 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. This statement establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are other than quoted prices included within Level 1 that are observable; Level 3 inputs are significant unobservable inputs. Investments that are measured at fair value using the net asset value per share (or its equivalent) as a practical expedient are not classified in the hierarchy below.

The following table summarizes the Cash Flow portfolio investments within the fair value hierarchy as of June 30, 2020:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Investments by fair value level				
Debt securities				
U.S. Treasuries	\$ 16,096,950	\$ 0	\$ 16,096,950	\$ 0
U.S. Treasury STRIPS	113,005,441	0	113,005,441	0
U.S. Agencies	332,188,310	0	332,188,310	0
Investment Grade Corporates	677,038,061	0	677,038,061	0
High Yield Corporates	9,802,661	0	9,802,661	0
Agency Mortgage-Backed Securities	96,594,835	0	96,594,835	0
Total debt securities	<u>1,244,726,258</u>	<u>0</u>	<u>1,244,726,258</u>	<u>0</u>
Total investments by fair value level	<u>1,244,726,258</u>	<u>\$ 0</u>	<u>\$ 1,244,726,258</u>	<u>\$ 0</u>
Investments measured at the net asset value (NAV)				
Short Term Investment Funds	1,428,192,591			
Total investments measured at the NAV	<u>1,428,192,591</u>			
Total investments measured at the fair value	<u>\$ 2,672,918,849</u>			

The Cash Flow portfolio did not hold any Level 1 or Level 3 investments as of June 30, 2020.

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 the various pricing vendors for these securities. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices.

The Cash Flow portfolio 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 or securities as determined and reported by the fund manager.

The following table summarizes the fair value, unfunded commitments, and redemption rules of those investments as of June 30, 2020:

	Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
Short Term Investment Funds ^(a)	\$ 1,428,192,591		Daily	0 days
Investments measured at the net asset value (NAV)	<u>\$ 1,428,192,591</u>			

a. *Short Term Investment Funds.* This type includes investments in three open-end mutual funds that invest exclusively 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.

5. Rate of Return:

The percentage rate of return for fiscal year 2020 for the Cash Flow portfolio was 2.3%. The percentage was derived by dividing the total investment income by the average daily investment balances.

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. During fiscal year 2020, no derivative instruments were utilized by the Cash Flow portfolio.

7. Proration of Investment Income and Fees:

The cash income received from pooled investments in the Cash Flow portfolio is prorated to state funds which have been certified as participating funds by the Legislative Appropriations Committee. The cash income is prorated to each individual participating fund using the ratio of its average daily cash balance to the total average daily cash balance of all funds. The income is distributed to the participating funds in the next fiscal year.

Per SDCL 4-5-30, the South Dakota Retirement System, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios' share of the SDIC fiscal year budgeted expenditures are transferred to the SDIC Operating Expense Fund. The Cash Flow and School and Public Lands portfolios' share of the SDIC fiscal year budgeted expenditures is deducted from the Cash Flow portfolio income and transferred to the SDIC Operating Expense Fund.

8. Commitments:

On June 30, 2020, the Cash Flow portfolio did not have any uncalled capital commitments.



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**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**

Executive Board
Legislative Research Council

and

Investment Council
State of 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 School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios, internal investment pools of the State of South Dakota, as of and for the year ended June 30, 2020, and the related notes to the financial statements, which collectively comprise the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios basic financial statements and have issued our report thereon dated October 2, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the South Dakota Investment Council'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 the South Dakota Investment Council's internal control. Accordingly, we do not express an opinion on the effectiveness of the South Dakota Investment Council'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 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 the South Dakota Investment Council's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, 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. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.



Russell A. Olson
Auditor General

October 2, 2020



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RUSSELL A. OLSON
AUDITOR GENERAL

INDEPENDENT AUDITOR'S REPORT

Executive Board
Legislative Research Council

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Investment Council
State of South Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios, internal investment pools of the State of South Dakota, as of and for the fiscal year ended June 30, 2020, and related notes to the financial statements, as listed in the table of contents.

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 opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the portfolios listed above as of June 30, 2020, and the changes in their financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As explained in the following table and in Note 2 to the financial statements, the financial statements include investments 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:

Portfolio	Amount	Percent of Net Position
School and Public Lands	\$ 47,689,661	15%
Dakota Cement Trust	\$ 52,401,101	16%
Education Enhancement Trust	\$ 88,821,909	15%
Health Care Trust	\$ 23,332,502	16%

The financial statements present only the above referenced investment portfolios managed by the South Dakota Investment Council and do not purport to, and do not, present fairly the financial position of the State of South Dakota as of June 30, 2020, the changes in its financial position, or, where applicable, its cash flows for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 2, 2020, on our consideration of the South Dakota Investment Council's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, 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 South Dakota Investment Council'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 South Dakota Investment Council's internal control over financial reporting and compliance.



Russell A. Olson
Auditor General

October 2, 2020

South Dakota Investment Council
Trust Portfolios
Statement of Net Position
As of June 30, 2020

	School and Public Lands Portfolio	Dakota Cement Trust Portfolio	Education Enhancement Trust Portfolio	Health Care Trust Portfolio
Assets				
Cash & cash equivalents	\$ 150,050	\$ 188,015	\$ 409,640	\$ 88,289
Receivables				
Investment income receivable	470,889	475,071	1,195,011	203,586
Unsettled investment sales	-	-	361,575	-
Total receivables	<u>470,889</u>	<u>475,071</u>	<u>1,556,586</u>	<u>203,586</u>
Investments, at fair value				
Short term investment fund	108,472,451	111,262,932	223,908,978	54,014,451
Fixed income	88,037,292	89,084,997	162,881,470	39,135,762
Equities	83,075,378	80,411,818	153,183,614	34,396,101
Alternative investments	47,689,661	52,401,101	88,821,909	23,332,502
Total investments	<u>327,274,782</u>	<u>333,160,848</u>	<u>628,795,971</u>	<u>150,878,816</u>
Total assets	<u>327,895,721</u>	<u>333,823,934</u>	<u>630,762,197</u>	<u>151,170,691</u>
Liabilities				
Unsettled investment purchases	24,985	14,991	49,970	4,997
Earnings distribution - declared	-	-	22,515,470	5,676,706
Total liabilities	<u>24,985</u>	<u>14,991</u>	<u>22,565,440</u>	<u>5,681,703</u>
Net Position	<u>\$ 327,870,736</u>	<u>\$ 333,808,943</u>	<u>\$ 608,196,757</u>	<u>\$ 145,488,988</u>

The accompanying notes are an integral part of the financial statements.

South Dakota Investment Council
Trust Portfolios
Statement of Changes in Net Position
For the fiscal year ended June 30, 2020

	School and Public Lands Portfolio	Dakota Cement Trust Portfolio	Education Enhancement Trust Portfolio	Health Care Trust Portfolio
Additions:				
Contributions	\$ 9,980,066	\$ -	\$ 8,442,139	\$ -
Investment income				
<i>From investing activities:</i>				
Net appreciation in fair value of investments	11,467,746	8,484,910	10,742,988	3,733,758
Interest	3,736,459	4,096,085	7,732,306	1,783,237
Dividends	2,610,104	2,664,626	5,037,057	1,149,445
Real estate income	479,472	516,604	887,184	222,424
Investment income	18,293,781	15,762,225	24,399,535	6,888,864
Less investment activity expense	(798,466)	(1,100,637)	(2,036,588)	(483,360)
Net investment activity income	17,495,315	14,661,588	22,362,947	6,405,504
<i>From securities lending activities:</i>				
Securities lending income	49,856	14,348	21,000	10,745
Securities lending expenses	(14,950)	(4,300)	(6,295)	(3,219)
Net securities lending activity income	34,906	10,048	14,705	7,526
Total investment income	17,530,221	14,671,636	22,377,652	6,413,030
Total additions	27,510,287	14,671,636	30,819,791	6,413,030
Deductions:				
Statutorily required distributions	16,120,981	13,004,590	22,515,470	5,676,706
Total deductions	16,120,981	13,004,590	22,515,470	5,676,706
Net increase in net position	11,389,306	1,667,046	8,304,321	736,324
Net position - Beginning of year	316,481,430	332,141,897	599,892,436	144,752,664
Net position - End of year	\$ 327,870,736	\$ 333,808,943	\$ 608,196,757	\$ 145,488,988

The accompanying notes are an integral part of the financial statements.

SOUTH DAKOTA INVESTMENT COUNCIL
TRUST PORTFOLIOS
NOTES TO THE FINANCIAL STATEMENTS

1. Reporting Entity:

The South Dakota Investment Council (SDIC) is a principal, functional sub-unit of state government. The SDIC is responsible for the investment of the state's monies in the state treasury. The SDIC provides investment management services on a prefunded cost recovery basis as authorized by South Dakota Codified Law (SDCL) 4-5-30.

The statements represent the financial activity of the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios. The statements report investments by each portfolio. The School and Public Lands portfolio represents assets held in permanent school funds. The Dakota Cement Trust portfolio represents proceeds from the sale of the South Dakota Cement Plant. The Education Enhancement Trust portfolio represents assets held in trust from the master settlement agreement between the State of South Dakota and major United States tobacco product manufacturers and other funds. The Health Care Trust portfolio represents assets held in trust from federal reimbursement for Medicaid and Medicare costs associated with publicly owned and operated nursing facilities.

2. Summary of Significant Accounting Policies:

a. Basis of Presentation:

The accompanying financial statements of the investment activity of the SDIC on behalf of the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios are prepared in accordance with generally accepted accounting principles (GAAP) for governments as prescribed by the Governmental Accounting Standards Board (GASB).

b. Basis of Accounting:

The statements for the portfolios are reported on the full accrual basis of accounting. Under this method, revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred. Security transactions and the related gains and losses are recorded on a trade date basis using the average cost method. Purchases and sales of foreign investments and the related income are translated at the rate of exchange on the respective transaction dates. Realized and unrealized gains and losses resulting from foreign currency changes are included in the Statement of Changes in Net Position. Dividend income is recorded on the ex-dividend date and interest income is accrued as earned.

c. Cash and Cash Equivalents:

Cash includes demand deposits and foreign currency cash balances. Foreign currency cash balances are translated into United States Dollars (USD) using the year-end spot foreign currency exchange rates.

d. Valuation of Securities:

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.

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 or securities 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 4: Fair Value Measurement.

Alternative investments, which consist of investments in a variety of markets and industries through limited partnerships, are valued as Level 3 on the fair value hierarchy or at NAV. These fair value estimates are subjective and based on judgment. The alternative investments fair values as a percentage of net position as of June 30, 2020 for School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios were 15%, 16%, 15%, and 16%, respectively.

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.

e. Use of Estimates:

The preparation of financial statements in accordance with GAAP requires management to make estimates that affect the reported amounts of net position as of June 30, 2020. Actual results could differ from those estimates.

f. New GAAP Implementation:

Government Accounting Standards Board did not issue any new or updated statements that affected SDIC for fiscal year 2020.

3. Deposits, Investments and Securities Lending:

The State Investment Officer is responsible for the investment of state public funds. The portfolios are governed by the prudent man rule; that is, the SDIC should use the same degree of care as a prudent man. The SDIC dictates the limits on the percentages the portfolios invest in various asset classes.

Deposits:

Custodial Credit Risk. 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 in the possession of an outside party. The SDIC has a formal deposit policy specific to custodial credit risk for the global equity portfolios of School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust. The policy states that the USD equivalent of any non-USD currency cannot exceed 2.0% of the portfolio fair value on a trade date + 5 calendar day basis. As of June 30, 2020, the portfolios had bank balances in various foreign currencies. These deposits are not collateralized or covered by depository insurance. As a result, the following amounts were exposed to custodial credit risk:

	School & Public Lands Portfolio	Dakota Cement Trust Portfolio	Education Enhancement Trust Portfolio	Health Care Trust Portfolio
Foreign Currency Cash Balances	\$ 143,942	\$ 183,031	\$ 388,904	\$ 86,104

Investments:

Securities Lending. State statutes and the SDIC 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. The SDIC'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% of fair value plus accrued interest for corporate debt securities, 102% of fair value for U.S. equity securities and 105% of fair value for foreign securities except in the case of loans of foreign securities which are denominated and payable in USD, in which event the collateral required is 102% of fair value. The earnings generated from the collateral investments results in the gross earnings from lending activities, which is then split on a percentage basis with the lending agent.

The fair value of securities on loan as of June 30, 2020 and the collateral held on the same date is listed in the following table:

	School & Public Lands Portfolio	Dakota Cement Trust Portfolio	Education Enhancement Trust Portfolio	Health Care Trust Portfolio
Fair Value of Securities on Loan	\$ 6,626,366	\$ 2,485,856	\$ 4,873,451	\$ 1,140,070
Collateral Held	6,781,685	2,553,507	5,006,415	1,170,116
Collateral % Held	102.34%	102.72%	102.73%	102.64%

The School & Public Lands, Dakota Cement Trust, Education Enhancement Trust and Health Care Trust portfolios have no credit risk exposure to borrowers because the amounts the portfolios owe the borrowers exceed the amounts the borrowers owe the portfolios. The contract with the lending agent requires the agent to indemnify the portfolios 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 the SDIC or the borrower. The SDIC 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 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.

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. The SDIC's securities lending policies are detailed in the preceding Securities Lending section. As of June 30, 2020, the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios do not have custodial credit risk with regard to securities lending.

Interest Rate Risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. SDIC policy limits or establishes ranges for the durations of the investment grade fixed income portfolios. Modified duration estimates the sensitivity of a bond's price to interest rate changes. The investment grade fixed income portfolios of School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust are benchmarked to the duration of the FTSE Broad Investment Grade (BIG) Index. The fair value (in USD) and weighted modified duration (in years) of the portfolios as of June 30, 2020 are listed in the following table:

Investment Type	School & Public Lands Portfolio		Dakota Cement Trust Portfolio		Education Enhancement Trust Portfolio		Health Care Trust Portfolio	
	Fair Value	Wgtd. Mod. Dur.	Fair Value	Wgtd. Mod. Dur.	Fair Value	Wgtd. Mod. Dur.	Fair Value	Wgtd. Mod. Dur.
U.S. Treasury Bills	\$ 2,791,143	0.45	\$ 483,738	0.38	\$ 4,661,905	0.45	\$ 126,921	0.40
U.S. Treasury STRIPS	18,138,336	9.29	18,467,352	9.29	19,854,544	9.29	8,045,441	9.29
U.S. Agencies	1,710,747	6.65	1,741,948	6.66	1,871,958	6.66	759,256	6.66
Investment Grade Corporates	19,474,014	4.23	19,880,414	4.23	21,284,571	4.23	8,669,250	4.23
High Yield Corporates	479,305	1.22	487,228	1.22	523,869	1.22	211,924	1.22
High Yield Bond Mutual Fund	12,899,776	3.90	13,179,857	3.90	24,024,329	3.90	5,761,154	3.90
Agency Mortgage-Backed Securities	16,399,891	2.96	16,283,500	2.90	16,937,652	2.97	7,317,488	2.90
Non-Agency Mortgage-Backed Securities	16,144,080	0.69	18,560,960	0.70	30,431,908	0.69	8,244,328	0.67
Municipal Bonds					43,290,734	5.08		
TOTAL	<u>\$ 88,037,292</u>		<u>\$ 89,084,997</u>		<u>\$ 162,881,470</u>		<u>\$ 39,135,762</u>	
Portfolio modified duration		4.25		4.26		4.14		4.24

The School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios invest in mortgage-backed securities. These securities are sensitive to prepayments by mortgagees, which is likely in declining interest rate environments, which can reduce the value of these securities.

Credit Risk. Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. SDIC policy establishes a percentage range and a normal allocation to various credit risk categories. The SDIC sets the investment policy annually for the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios. This policy establishes the benchmark percentage invested in each asset category and the minimum and maximum range of each asset category. 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 (at fair value):

	School & Public Lands Portfolio	Dakota Cement Trust Portfolio	Education Enhancement Trust Portfolio	Health Care Trust Portfolio
Moody's rating:				
Aaa	\$ 122,155,205	\$ 126,009,391	\$ 242,824,482	\$ 60,649,545
Aa	5,664,475	5,868,551	23,495,950	2,565,913
A	6,397,663	6,557,415	22,360,781	2,824,764
Baa	8,107,226	8,228,381	9,076,859	3,589,243
Ba	980,754	1,075,458	1,460,641	469,530
B	1,961,855	2,337,744	3,822,364	1,047,599
Caa	2,890,449	3,304,927	5,505,927	1,479,739
Ca	3,075,364	3,521,960	5,795,019	1,590,736
C	424,455	495,963	807,445	239,303
Unrated	18,851,836	20,015,799	42,640,328	8,780,359
Total	<u>\$ 170,509,282</u>	<u>\$ 177,415,589</u>	<u>\$ 357,789,796</u>	<u>\$ 83,236,731</u>

Concentration of Credit Risk. Concentration of credit risk is the risk of loss that may be attributed to the magnitude of a government's investment in a single issuer. The SDIC does not have a formal policy in place to limit investments in any particular issuer for the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios. Additionally, there are no single issuer exposures (excluding those issued by or explicitly guaranteed by the U.S. Government, or involving mutual funds or investment pools) within the portfolios that comprise 5% of the overall portfolios as of June 30, 2020.

Foreign Currency Risk. Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit. The School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios' exposure to foreign currency risk derives from their positions in foreign currency and foreign currency-denominated equity investments. To match the unhedged benchmark, the SDIC's normal procedure is not to hedge foreign currency back to USD. SDIC's procedure does allow hedging under certain circumstances when deemed appropriate by the State

Investment Officer and portfolio manager. The portfolios' exposure to foreign currency risk as of June 30, 2020 was as follows (in USD fair values):

Currency	School & Public Lands Portfolio			Dakota Cement Trust Portfolio		
	Equities	Cash	Totals	Equities	Cash	Totals
Australian Dollar	\$ 197,420	\$ 36,209	\$ 233,629	\$ 208,952	\$ 45,981	\$ 254,933
British Pound	2,312,499	8,677	2,321,176	2,336,419	9,420	2,345,839
Canadian Dollar	839,000	3,329	842,329	833,510	33,934	867,444
Danish Krone	157,565	0	157,565	173,724	0	173,724
Euro	5,586,068	7,622	5,593,690	5,465,128	7,919	5,473,047
Hong Kong Dollar	134,749	62,333	197,082	138,581	55,521	194,102
Japanese Yen	2,533,475	16,761	2,550,236	2,573,700	22,812	2,596,512
Norwegian Krone	15,902	9,011	24,913	16,992	7,444	24,436
South Korean Won	1,139,459	0	1,139,459	1,136,076	0	1,136,076
Swedish Krona	117,985	0	117,985	116,716	0	116,716
Swiss Franc	2,708,501	0	2,708,501	2,669,422	0	2,669,422
Total	\$ 15,742,623	\$ 143,942	\$ 15,886,565	\$ 15,669,220	\$ 183,031	\$ 15,852,251

Currency	Education Enhancement Trust Portfolio			Health Care Trust Portfolio		
	Equities	Cash	Totals	Equities	Cash	Totals
Australian Dollar	\$ 403,939	\$ 91,385	\$ 495,324	\$ 90,747	\$ 20,370	\$ 111,117
British Pound	4,458,918	17,957	4,476,875	1,002,289	1,423	1,003,712
Canadian Dollar	1,573,430	65,949	1,639,379	352,978	15,241	368,219
Danish Krone	329,809	0	329,809	74,318	0	74,318
Euro	10,424,177	15,153	10,439,330	2,341,438	3,401	2,344,839
Hong Kong Dollar	267,286	110,264	377,550	58,967	25,762	84,729
Japanese Yen	4,942,427	73,889	5,016,316	1,110,191	16,679	1,126,870
Norwegian Krone	32,993	14,307	47,300	7,505	3,228	10,733
South Korean Won	2,194,910	0	2,194,910	492,360	0	492,360
Swedish Krona	222,458	0	222,458	50,027	0	50,027
Swiss Franc	5,098,180	0	5,098,180	1,146,716	0	1,146,716
Total	\$ 29,948,527	\$ 388,904	\$ 30,337,431	\$ 6,727,536	\$ 86,104	\$ 6,813,640

Investments with external managers, which are not included in the table above, may expose the portfolios to additional foreign currency risk. The fair values (in USD) of externally-managed real estate, private equity, and other fund investments as of June 30, 2020 were as follows:

	School & Public Lands Portfolio	Dakota Cement Trust Portfolio	Education Enhancement Trust Portfolio	Health Care Trust Portfolio
Real Estate Funds	\$ 28,571,924	\$ 30,516,727	\$ 52,817,465	\$ 13,575,764
Private Equity Funds	19,082,067	21,826,185	35,920,350	9,735,414
Other Funds	35,670	58,189	84,094	21,324
Total	\$ 47,689,661	\$ 52,401,101	\$ 88,821,909	\$ 23,332,502

4. Fair Value Measurement:

Investments are reported at fair value as of June 30, 2020, to the extent available. GASB Statement No. 72 – *Fair Value Measurement and Application*, defines fair value as 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. This statement establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are other than quoted prices included within Level 1 that are observable; Level 3 inputs are significant unobservable inputs. Investments that are measured at fair value using the net asset value per share (or its equivalent) as a practical expedient are not classified in the hierarchy below.

The following tables summarize the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolio investments within the fair value hierarchy as of June 30, 2020:

	School & Public Lands Portfolio			
	Total	Level 1	Level 2	Level 3
Investments by fair value level				
Debt securities				
U.S. Treasury Bills	\$ 2,791,143	\$ 0	\$ 2,791,143	\$ 0
U.S. Treasury STRIPS	18,138,336	0	18,138,336	0
U.S. Agencies	1,710,747	0	1,710,747	0
Investment Grade Corporates	19,474,014	0	19,474,014	0
High Yield Corporates	479,305	0	479,305	0
Agency Mortgage-Backed Securities	16,399,891	0	16,399,891	0
Non-Agency Mortgage-Backed Securities	16,144,080	0	16,144,080	0
Total debt securities	75,137,516	0	75,137,516	0
Equity securities				
Domestic Stock	52,271,430	52,271,430	0	0
Depository Receipts	778,077	778,077	0	0
ETF - Exchange Traded Funds	14,255,846	14,255,846	0	0
International Stock	15,742,623	15,742,623	0	0
Stock Rights	27,402	27,402	0	0
Total equity securities	83,075,378	83,075,378	0	0
Alternative Investments				
Other Funds	0	0	0	0
Total alternative investments	0	0	0	0
Total investments by fair value level	158,212,894	\$ 83,075,378	\$ 75,137,516	\$ 0
Investments measured at the net asset value (NAV)				
Short Term Investment Funds	108,472,451			
High Yield Bond Mutual Funds	12,899,776			
Alternative investments				
Real Estate Funds	28,571,924			
Private Equity Funds	19,082,067			
Other Funds	35,670			
Total alternative investments	47,689,661			
Total Investments measured at the NAV	169,061,888			
Total Investments measured at the fair value	\$ 327,274,782			

	Dakota Cement Trust Portfolio			
	Total	Level 1	Level 2	Level 3
Investments by fair value level				
Debt securities				
U.S. Treasury Bills	\$ 483,738	\$ 0	\$ 483,738	\$ 0
U.S. Treasury STRIPS	18,467,352	0	18,467,352	0
U.S. Agencies	1,741,948	0	1,741,948	0
Investment Grade Corporates	19,880,414	0	19,880,414	0
High Yield Corporates	487,228	0	487,228	0
Agency Mortgage-Backed Securities	16,283,500	0	16,283,500	0
Non-Agency Mortgage-Backed Securities	18,560,960	0	18,560,960	0
Total debt securities	75,905,140	0	75,905,140	0
Equity securities				
Domestic Stock	52,824,006	52,824,006	0	0
Depository Receipts	747,909	747,909	0	0
ETF - Exchange Traded Funds	11,143,368	11,143,368	0	0
International Stock	15,669,220	15,669,220	0	0
Stock Rights	27,315	27,315	0	0
Total equity securities	80,411,818	80,411,818	0	0
Alternative Investments				
Other Funds	0	0	0	0
Total alternative investments	0	0	0	0
Total investments by fair value level	156,316,958	\$ 80,411,818	\$ 75,905,140	\$ 0
Investments measured at the net asset value (NAV)				
Short Term Investment Funds	111,262,932			
High Yield Bond Mutual Funds	13,179,857			
Alternative investments				
Real Estate Funds	30,516,727			
Private Equity Funds	21,826,185			
Other Funds	58,189			
Total alternative investments	52,401,101			
Total Investments measured at the NAV	176,843,890			
Total Investments measured at the fair value	\$ 333,160,848			

	Education Enhancement Trust Portfolio			
	Total	Level 1	Level 2	Level 3
Investments by fair value level				
Debt securities				
U.S. Treasury Bills	\$ 4,661,905	\$ 0	\$ 4,661,905	\$ 0
U.S. Treasury STRIPS	19,854,544	0	19,854,544	0
U.S. Agencies	1,871,958	0	1,871,958	0
Investment Grade Corporates	21,284,571	0	21,284,571	0
High Yield Corporates	523,869	0	523,869	0
Agency Mortgage-Backed Securities	16,937,652	0	16,937,652	0
Non-Agency Mortgage-Backed Securities	30,431,908	0	30,431,908	0
Municipal Bonds	43,290,734	0	43,290,734	0
Total debt securities	138,857,141	0	138,857,141	0
Equity securities				
Domestic Stock	100,661,350	100,661,350	0	0
Depository Receipts	1,428,582	1,428,582	0	0
ETF - Exchange Traded Funds	21,092,350	21,092,350	0	0
International Stock	29,948,527	29,948,527	0	0
Stock Rights	52,805	52,805	0	0
Total equity securities	153,183,614	153,183,614	0	0
Alternative Investments				
Other Funds	0	0	0	0
Total alternative investments	0	0	0	0
Total investments by fair value level	292,040,755	\$ 153,183,614	\$ 138,857,141	\$ 0
Investments measured at the net asset value (NAV)				
Short Term Investment Funds	223,908,978			
High Yield Bond Mutual Funds	24,024,329			
Alternative investments				
Real Estate Funds	52,817,465			
Private Equity Funds	35,920,350			
Other Funds	84,094			
Total alternative investments	88,821,909			
Total Investments measured at the NAV	336,755,216			
Total Investments measured at the fair value	\$ 628,795,971			

	Health Care Trust Portfolio			
	Total	Level 1	Level 2	Level 3
Investments by fair value level				
Debt securities				
U.S. Treasury Bills	\$ 126,921	\$ 0	\$ 126,921	\$ 0
U.S. Treasury STRIPS	8,045,441	0	8,045,441	0
U.S. Agencies	759,256	0	759,256	0
Investment Grade Corporates	8,669,250	0	8,669,250	0
High Yield Corporates	211,924	0	211,924	0
Agency Mortgage-Backed Securities	7,317,488	0	7,317,488	0
Non-Agency Mortgage-Backed Securities	8,244,328	0	8,244,328	0
Total debt securities	33,374,608	0	33,374,608	0
Equity securities				
Domestic Stock	22,589,485	22,589,485	0	0
Depository Receipts	321,166	321,166	0	0
ETF - Exchange Traded Funds	4,745,957	4,745,957	0	0
International Stock	6,727,536	6,727,536	0	0
Stock Rights	11,957	11,957	0	0
Total equity securities	34,396,101	34,396,101	0	0
Alternative Investments				
Other Funds	0	0	0	0
Total alternative investments	0	0	0	0
Total investments by fair value level	67,770,709	\$ 34,396,101	\$ 33,374,608	\$ 0
Investments measured at the net asset value (NAV)				
Short Term Investment Funds	54,014,451			
High Yield Bond Mutual Funds	5,761,154			
Alternative investments				
Real Estate Funds	13,575,764			
Private Equity Funds	9,735,414			
Other Funds	21,324			
Total alternative investments	23,332,502			
Total Investments measured at the NAV	83,108,107			
Total Investments measured at the fair value	\$ 150,878,816			

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.

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 the various pricing vendors for these securities. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices.

The Other Fund classified in Level 3 of the fair value hierarchy is valued at zero. It is an investment in an alternative investment fund that invested in distressed and defaulted debt securities and equities of financially troubled companies. All positions in the fund have been liquidated and only cash remains. The fund holds contingent liabilities that offset cash. Due to the highly questionable outcome of the contingent liabilities it has been determined that a value of zero best reflects the fair value considering the information available as of June 30, 2020.

The School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios hold shares or interests 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 or securities as determined and reported by the fund manager or general partner.

The following tables summarize the fair value, unfunded commitments, and redemption rules of those investments as of June 30, 2020:

	School & Public Lands Portfolio			
	Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
Short Term Investment Funds ^(a)	\$ 108,472,451		Daily	0 days
High Yield Bond Mutual Funds ^(b)	12,899,776		Daily	1 day
Alternative investments				
Real Estate Funds ^(c)	28,571,924	\$ 25,734,018		
Private Equity Funds ^(d)	19,082,067	7,951,768		
Other Funds ^(e)	35,670			
Total alternative investments	<u>47,689,661</u>			
Investments measured at the net asset value (NAV)	<u>\$ 169,061,888</u>			

	Dakota Cement Trust Portfolio			
	Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
Short Term Investment Funds ^(a)	\$ 111,262,932		Daily	0 days
High Yield Bond Mutual Funds ^(b)	13,179,857		Daily	1 day
Alternative investments				
Real Estate Funds ^(c)	30,516,727	\$ 26,735,904		
Private Equity Funds ^(d)	21,826,185	8,871,248		
Other Funds ^(e)	58,189			
Total alternative investments	<u>52,401,101</u>			
Investments measured at the net asset value (NAV)	<u>\$ 176,843,890</u>			

Education Enhancement Trust Portfolio				
	Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
Short Term Investment Funds ^(a)	\$ 223,908,978		Daily	0 days
High Yield Bond Mutual Funds ^(b)	24,024,329		Daily	1 day
Alternative investments				
Real Estate Funds ^(c)	52,817,465	\$ 48,439,788		
Private Equity Funds ^(d)	35,920,350	15,212,953		
Other Funds ^(e)	84,094			
Total alternative investments	<u>88,821,909</u>			
Investments measured at the net asset value (NAV)	<u>\$ 336,755,216</u>			

Health Care Trust Portfolio				
	Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
Short Term Investment Funds ^(a)	\$ 54,014,451		Daily	0 days
High Yield Bond Mutual Funds ^(b)	5,761,154		Daily	1 day
Alternative investments				
Real Estate Funds ^(c)	13,575,764	\$ 11,628,728		
Private Equity Funds ^(d)	9,735,414	3,959,891		
Other Funds ^(e)	21,324			
Total alternative investments	<u>23,332,502</u>			
Investments measured at the net asset value (NAV)	<u>\$ 83,108,107</u>			

a. Short Term Investment Funds. This type includes investments in one open-end mutual fund that invests exclusively 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 value of the investment in this type has been determined using the NAV per share of the investment.

b. High Yield Bond Mutual Funds. This type includes an investment in one open-end mutual fund that invests mainly in a diversified group of high-yielding, higher risk corporate bonds with medium- and lower-range credit-quality ratings. The fair value of the investment in this type has been determined using the NAV per share of the investment.

c. Real Estate Funds. This type includes seventeen 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.

d. Private Equity Funds. This type includes twelve 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.

e. Other Funds. This type includes one other alternative investment that is a hybrid private equity hedge fund that invests primarily in a broad range of debt, debt-related, and real estate-related investments. The fair value 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 fund. Distributions from the fund will be received as the underlying investments of the fund 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.

5. Rate of Return:

The percentage rates of return for fiscal year 2020 for the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios were 5.6%, 4.5%, 3.7%, and 4.4%, respectively. The percentages were derived using the net-of-fee time-weighted rate of return calculation and the geometric linking of those returns.

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. The School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios may be exposed to various derivative products through the investment management of the SDIC and its external managers. During fiscal year 2020, no derivative instruments were utilized by SDIC in the internally-managed portfolios.

7. Statutorily Required Distributions:

The cash income received from investments in the School and Public Lands portfolio is received and deposited into the trust fund. Annual distributions of the receipted income are distributed to the permanent school and other educational and charitable funds administered by the Commissioner of School and Public Lands.

The cash income from investments in the Dakota Cement Trust portfolio is received and deposited into the trust fund. By June 30th, annual distributions of four percent of the lesser of the average fair value of the sixteen most recent calendar quarter ends as of the prior December 31st or the fair value as of the prior December 31st are made from the Dakota Cement Trust to the State General Fund.

The cash income from investments in the Education Enhancement Trust and Health Care Trust portfolios is received and deposited into the respective trust funds. At the beginning of each fiscal year, amounts equal to four percent of the average fair value at the end of the sixteen most recent calendar quarter ends as of the prior December 31st are transferred from the Education Enhancement Trust and the Health Care Trust portfolios to the State General Fund. The transfer amount cannot invade the principal of either trust.

8. Commitments:

As of June 30, 2020, the School and Public Lands, Dakota Cement Trust, Education Enhancement Trust, and Health Care Trust portfolios had uncalled capital commitments to private equity and real estate limited partnerships funds. The commitments may be called at the discretion of the general partner or may never be called. As capital is called, it is funded from capital and earnings returned by the limited partnerships or from other assets. In addition to the uncalled commitments reported in Note 4, the following amounts include uncalled commitments for funds established as of June 30, 2020 that have not yet provided an NAV (or its equivalent) of the portfolio's ownership interest or called capital. Approximate uncalled capital commitments as of June 30, 2020 were as follows:

	School & Public Lands Portfolio	Dakota Cement Trust Portfolio	Education Enhancement Trust Portfolio	Health Care Trust Portfolio
Real Estate Funds	\$ 25,734,018	\$ 26,735,904	\$ 48,439,788	\$ 11,628,728
Private Equity Funds	16,133,533	16,740,698	30,627,224	7,319,986
Total	<u>\$ 41,867,551</u>	<u>\$ 43,476,602</u>	<u>\$ 79,067,012</u>	<u>\$ 18,948,714</u>