



TEACHERS' RETIREMENT SYSTEM

of the State of Kentucky

BOARD OF TRUSTEES

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GARY L. HARBIN, CPA
Executive Secretary

Regular Quarterly Meeting of the
TRS Board of Trustees

A G E N D A

September 18, 2017, 12:30 p.m.

Board Called to Order

Roll Call

1. Reports for Consent

1.1. Consideration/Approval of Minutes

1.1.1. Quarterly Meeting of the Board of Trustees held June 19, 2017

1.1.2. Special Meeting of the Governance and Audit Committee held
June 19, 2017

1.1.3. Special Meeting of the Insurance Committee held June 19, 2017

1.2. Applications for Retirement and Annuity

1.3. Survivor Benefits

1.4. Life Insurance Benefits

1.5. Refunds

1.6. Interim Financial Statements

2. Report of the Investment Committee

3. Report of the Insurance Committee

4. Executive Secretary's Observations and Comments

General Discussion

Adjournment

The meeting will take place in the boardroom at the offices of the
Teachers' Retirement System of Kentucky, 479 Versailles Road,
Frankfort, Kentucky.

TO: Board of Trustees of the
Teachers' Retirement System of Kentucky

FROM: Gary L. Harbin, CPA
Executive Secretary

DATE: September 18, 2017

SUBJECT: Reports for Consent

1.1. Consideration/Approval of Minutes

1.1.1. Quarterly Meeting of the Board of Trustees held June 19, 2017

1.1.2. Special Meeting of the Governance and Audit Committee held June 19, 2017

1.1.3. Special Meeting of the Insurance Committee held June 19, 2017

1.2. Applications for Retirement and Annuity

The lists of members who retired June, July and August 2017 will be available for examination at the meeting. Attached is a summary of the particular payments and a comparison to the same period last year. Initial retirements for the period included 1,460 retirees with monthly payments totaling \$4,841,114.18. During the same period last year, there were 1,488 retirements with monthly payments totaling \$4,914,246.59.

Recommendation: The board is requested to approve the initial payments listed in the report.

1.3. Survivor Benefits

The list of persons qualifying for survivor benefit payments for the quarter April 1, 2017 through June 30, 2017 will be available for examination at the meeting. During the period, there were 18 survivor benefits with a total monthly payment of \$6,984.81.

Recommendation: The board is requested to approve the survivor benefit payments for the period April 1, 2017 through June 30, 2017 as listed in the report.

1.4. Life Insurance Benefits

The list of payments of life insurance benefits due to death of active and retired teachers for the period April 1, 2017 through June 30, 2017 will be available for examination at the meeting. There were 6 payments to the estates or beneficiaries of active teachers and 252 payments to the estates or beneficiaries of retired teachers for total payments of \$1,272,000. During the same quarter in 2016, there were 229 payments in the amount of \$1,130,000.

Recommendation: The board is requested to approve the payment of life insurance benefits as listed in the report.

1.5. Refunds

The report of refunds for the quarter ended June 30, 2017 is also attached. There were 397 refunds for the quarter April 1, 2017 through June 30, 2017, and the amount refunded was \$3,722,435.68. The refunds are for the following categories:

Regular withdrawals	374	\$3,461,053.78
Deaths	<u>23</u>	<u>\$ 261,381.90</u>
Totals	397	\$3,722,435.68

During the same quarter in 2016 there were 394 refunds totaling \$3,130,953.15.

Recommendation: The board is requested to approve the payment of refunds as listed in the report.

1.6. Interim Financial Statements

Attached are the Interim Financial Statements for the quarter ended June 30, 2017.

Recommendation: The Interim Financial Statements are provided for informational purposes only and require no action by the board.

Teachers' Retirement System of Kentucky
Initial Applications for Retirement and Annuity
2017

	June	July	August	Total	Same Period 2016
Handicapped Child	<i>0</i> \$0.00	<i>0</i> \$0.00	<i>0</i> \$0.00	<i>0</i> \$0.00	<i>0</i> \$0.00
Disability Retirement	<i>9</i> \$24,823.81	<i>28</i> \$75,825.49	<i>18</i> \$51,138.35	<i>55</i> \$151,787.65	<i>59</i> \$161,767.91
Service Retirement	<i>389</i> \$1,221,343.84	<i>828</i> \$2,927,170.32	<i>188</i> \$540,812.37	<i>1,405</i> \$4,689,326.53	<i>1,427</i> \$4,743,683.02
Beneficiary of Member Eligible to Retire	<i>0</i> \$0.00	<i>0</i> \$0.00	<i>0</i> \$0.00	<i>0</i> \$0.00	<i>2</i> \$8,795.66
TOTALS	<i>398</i> \$1,246,167.65	<i>856</i> \$3,002,995.81	<i>206</i> \$591,950.72	<i>1,460</i> \$4,841,114.18	<i>1,488</i> \$4,914,246.59

Reports for Consent
Member Account Refunds
For the period April 2017 - June 2017

Active Refunds	Count	Net Refund	Taxes Withheld	Rollovers	Total
April	148	604,791.35	150,712.37	653,972.16	1,409,475.88
May	153	649,886.23	162,379.99	692,253.53	1,504,519.75
June	74	333,920.60	83,480.23	129,657.32	547,058.15
Total	374				3,461,053.78

Deceased Refunds	Count	Net Refund	Taxes Withheld	Rollovers	Total
April	6	25,482.85	6,370.70	0.00	31,853.55
May	10	123,730.93	12,788.14	41,303.29	177,822.36
June	7	4,908.91	64.80	46,732.28	51,705.99
Total	23				261,381.90

Total Refunds	Count	Net Refund	Taxes Withheld	Rollovers	Total
April	154	630,274.20	157,083.07	653,972.16	1,441,329.43
May	163	773,617.16	175,168.13	733,556.82	1,682,342.11
June	81	338,829.51	83,545.03	176,389.60	598,764.14
Total	397				3,722,435.68

TEACHERS' RETIREMENT SYSTEM

OF THE STATE OF KENTUCKY



INTERIM FINANCIAL STATEMENTS

QUARTER ENDED JUNE 30, 2017
(UNAUDITED)

Statements of Plan Net Assets
as of June 30, 2017 and 2016
(Book Basis - Unadjusted)

	Defined Benefit Plan		Health Insurance Plans		Life Insurance Plan		Other Funds		TOTAL	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
ASSETS										
Cash	\$ 137,375,589	\$ 15,245,731	\$ 87,841,753	\$ 59,843,503	\$ 187,657	\$ -	\$ 23,852	\$ 481	\$ 225,428,851	\$ 75,089,715
Receivables										
Contributions	28,779,827	34,664,070	18,456,779	21,525,458	105,264	95,285			47,341,870	56,284,813
State of Kentucky	13,640,427	22,766,523	7,592,074	1,359,808	32,617	54,392			21,265,118	24,180,723
Investment Income	40,623,372	39,619,872	1,685,597	1,333,953	1,036,228	1,090,402	2,693	2,417	43,347,890	42,046,644
Investment Sales Receivable	49,973,750	18,182,733	915,100	633,642	-	-			50,888,850	18,816,375
Installment Account Receivable	366,602	478,909							366,602	478,909
Other Receivables	71,701	81,004	17,944,004	33,476,310					18,015,705	33,557,314
Due from Other Funds	1,567,471	3,719,997							1,567,471	3,719,997
Total Receivables	135,023,150	119,513,108	46,593,554	58,329,171	1,174,109	1,240,079	2,693	2,417	182,793,506	179,084,775
Investments at Book Value										
Short Term Investments	521,348,979	507,724,995	46,008,715	18,186,505	4,150,027	587,582	398,093	410,591	571,905,814	526,909,673
Bonds and Mortgages	2,758,485,338	2,522,518,198	69,833,179	60,538,361	78,977,060	83,238,362	199,485	199,485	2,907,495,062	2,666,494,406
Stocks	8,089,204,832	8,189,105,062	343,056,259	287,013,598			185,574	185,574	8,432,446,665	8,476,304,234
Alternative Investments	853,371,797	781,608,594	34,118,194	21,817,665					887,489,991	803,426,259
Real Estate	906,726,070	818,009,983	38,850,944	23,335,135					945,577,014	841,345,118
Additional Categories	1,383,696,857	1,320,064,061	157,097,353	140,834,268					1,540,794,210	1,460,898,329
Total Investments	14,512,833,873	14,139,030,893	688,964,644	551,725,532	83,127,087	83,825,944	783,152	795,650	15,285,708,756	14,775,378,019
Capital Assets	18,046,639	16,973,670							18,046,639	16,973,670
(net of accumulated depreciation)										
Total Assets	14,803,279,251	14,290,763,402	823,399,951	669,898,206	84,488,853	85,066,023	809,697	798,548	15,711,977,752	15,046,526,179
LIABILITIES										
Liabilities										
Accounts Payable	2,201,644	1,917,838	10,300	19,811					2,211,944	1,937,649
Investment Purchases Payable	76,193,228	16,052,683	3,043,724	1,425,467			-	-	79,236,952	17,478,150
Investment Fees Payable	15,983,153	11,447,198	796,350	709,100			-	-	16,779,503	12,156,298
Due to Other Funds	-	1,935,385	1,538,574	1,747,115	27,690	36,837	1,208	661	1,567,472	3,719,998
Revenues Collected in Advance	-	-	555,554	2,042,315					555,554	2,042,315
Total Liabilities	94,378,025	31,353,104	5,944,502	5,943,808	27,690	36,837	1,208	661	100,351,425	37,334,410
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS	\$ 14,708,901,226	\$ 14,259,410,298	\$ 817,455,449	\$ 663,954,398	\$ 84,461,163	\$ 85,029,186	\$ 808,489	\$ 797,887	\$ 15,611,626,327	\$ 15,009,191,769

Statements of Changes in Plan Net Assets
For the Twelve Months Ended June 30, 2017 and 2016
(Book Basis - Unadjusted)

	Defined Benefit Plan		Medical Insurance Plan		Life Insurance Plan		Other Funds		TOTAL	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
ADDITIONS										
Contributions										
Employer- State Paid	\$ 981,417,089	\$ 484,986,954	\$ 75,496,731	\$ 74,367,250	\$ 881,703	\$ 872,990	\$ -	\$ -	\$ 1,057,795,523	\$ 560,227,194
Employer- LSD, Other	79,302,904	80,467,636	104,879,255	104,347,841	167,980	164,779	220,001	-	184,570,140	184,980,256
Member- Active	313,625,434	313,044,226	128,697,000	127,757,426					442,322,434	440,801,652
Member- Retired			58,064,211	56,531,068					58,064,211	56,531,068
Recovery Income			54,650,586	56,695,115					54,650,586	56,695,115
Total Contribution	1,374,345,427	878,498,816	421,787,783	419,698,700	1,049,683	1,037,769	220,001	-	1,797,402,894	1,299,235,285
Investment Income (at book value)										
Net Gain/(Loss) on Investment Sales	721,670,366	287,614,385	13,071,369	(8,654,380)	557,704	(728)	-	-	735,299,439	278,959,277
Interest	153,207,310	162,339,804	5,777,776	8,029,465	3,011,187	3,095,887	10,920	10,013	162,007,193	173,475,169
Dividends	180,297,227	194,570,308	3,787,309	1,207,958			5,468	5,187	184,090,004	195,783,453
Rental Income, Net	30,477,797	28,039,967							30,477,797	28,039,967
Securities Lending, Net	2,559,933	1,937,053			2,584	2,485	162	283	2,562,679	1,939,821
Gross Investment Income	1,088,212,633	674,501,517	22,636,454	583,043	3,571,475	3,097,644	16,550	15,483	1,114,437,112	678,197,687
Less Investment Expense	(57,836,050)	(47,864,404)	(3,170,868)	(2,280,393)	(10,478)	(11,440)	(114)	(120)	(61,017,510)	(50,156,357)
Net Investment Income	1,030,376,583	626,637,113	19,465,586	(1,697,350)	3,560,997	3,086,204	16,436	15,363	1,053,419,602	628,041,330
Total Additions	2,404,722,010	1,505,135,929	441,253,369	418,001,350	4,610,680	4,123,973	236,437	15,363	2,850,822,496	1,927,276,615
DEDUCTIONS										
Benefits	1,918,612,128	1,833,198,630			5,151,013	4,595,489	224,628	94,665	1,923,987,769	1,837,888,784
Refunds of Contributions	26,305,240	27,747,742							26,305,240	27,747,742
Under 65 Insurance Expenses			119,200,444	127,673,325					119,200,444	127,673,325
Over 65 Insurance Expenses			167,013,299	157,266,179					167,013,299	157,266,179
Administrative Expense	10,313,715	10,061,909	1,538,574	1,686,070	27,690	27,195	1,208	560	11,881,187	11,775,734
Total Deductions	1,955,231,083	1,871,008,281	287,752,317	286,625,574	5,178,703	4,622,684	225,836	95,225	2,248,387,939	2,162,351,764
Net Increase (Decrease)	449,490,927	(365,872,352)	153,501,052	131,375,776	(568,023)	(498,711)	10,601	(79,862)	602,434,557	(235,075,149)
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS										
Beginning of year	14,259,410,299	14,625,282,650	663,954,397	532,578,622	85,029,186	85,527,897	797,888	877,749	15,009,191,770	15,244,266,918
Ending of period	\$ 14,708,901,226	\$ 14,259,410,298	\$ 817,455,449	\$ 663,954,398	\$ 84,461,163	\$ 85,029,186	\$ 808,489	\$ 797,887	\$ 15,611,626,327	\$ 15,009,191,769

TO: Board of Trustees of the
Teachers' Retirement System of Kentucky

FROM: Gary L. Harbin, CPA
Executive Secretary

DATE: September 18, 2017

SUBJECT: Report of the Investment Committee

1. Investment Committee Meeting and Actions: The investments approved at the August 24, 2017 Investment Committee meeting are as follows: \$50 million from the Retirement Annuity Trust Fund and \$10 million from the Medical Insurance Trust Fund to the Carlyle Asia Partners V LP Fund. Additionally, outside managers Columbia Threadneedle High Yield, Fort Washington Private Equity, and Fort Washington Focused Equity reported to the Committee on their respective portfolios.

2. Purchases and Disposals: The Report of the Investment Committee for the quarter ended June 30, 2017 is presented for review and approval. During this quarter, there were 2,088 purchases amounting to \$2,670,643,530.93 and 2,927 disposals amounting to \$2,550,144,372.82. The disposals consisted of 2,551 sales, 334 principal payments and 42 redemptions. While the TRS investment office initiates each of these transactions, the custodian of securities is responsible for handling and securing each stock, bond or other type of investment. At the end of the quarter, TRS's invested securities had a book value of \$14,615,776,256.27 and a market value of \$18,617,890,295.13.

3. Staff's comments on the economic and market conditions: Global risk assets continued to perform well during the quarter ending June 30, 2017, with gains broadly supported by strengthening economic data related to global inflation, job growth and corporate fundamentals. In contrast to prior run-ups in risk assets, the past quarter was marked by high levels of sector and market factor dispersion. This created significant opportunities for skilled active managers and generated tailwinds for strategies with heavy growth and cyclical biases. Geographically, emerging markets outperformed developed, while international markets generally outperformed US markets.

Gains across most risk assets occurred despite persistent political divisiveness in the US, heightened geopolitical risks and a range of other international issues. Although positive economic fundamentals have thus far supported 2017 market gains, it is possible that unanticipated global central bank policy and US political events could have a larger influence on markets through the remainder of the year.

US interest rates experienced heightened volatility during the quarter before abruptly rising in the last week. Given expectations of additional actions by central banks over the next several quarters, volatility of global rates may remain high, which could lead to headwinds for longer-duration strategies.

Domestic equity markets continued to rally during the second quarter, albeit at a slower rate and with less volatility. Expectations for fiscal stimulus were again supportive of markets during the quarter, as was the positive tone from the Federal Open Market Committee (FOMC) regarding near-term economic growth and inflation expectations. Equities provided positive returns across all market caps and styles, but with significant dispersion across sectors and market factors.

In some ways, US equity performance thus far in 2017 represented a reversal of the trend experienced during the same period in 2016. During the first half of 2016, low volatility sectors and securities viewed as “bond proxies” performed well. In contrast, 2017 has proven to be more favorable for high momentum, high growth areas of the market. At minimum, this rapid market rotation illustrates the importance of establishing sufficient factor diversification to dampen portfolio volatility.

International equity markets continued to react positively to signs of strengthening economic growth across both developed and emerging markets, driving equity prices and sovereign debt yields higher. As in the US, international growth equity broadly outperformed value. Developed small-cap equities outperformed large-cap equities, while emerging markets equities narrowly edged out developed markets equities. As would be expected during periods of growth leadership, healthcare and technology led performance from a sector standpoint, with materials, energy and telecom lagging.

From a country perspective, political developments drove a generally risk-on repricing of assets. France and the Netherlands withstood the anti-globalization political forces, which reduced political uncertainty and supported higher asset prices. Italy likewise benefited from political tailwinds, as it successfully closed two failed banks without experiencing broader contagion in the financial sector. The outlook for non-US equities by most market participants appears to be cautiously optimistic. Supportive developments include reduced political uncertainty and positive indicators of GDP and earnings growth. This, coupled with more reasonable valuations in comparison to the US, supported the ACW ex US Index’s 300 bps of quarterly outperformance versus the Russell 3000.

The FOMC raised the Federal Funds rate by 0.25% during its June meeting, citing developments in labor markets and expectations for higher inflation over the near-term. FOMC statements and minutes from previous meetings suggest the committee believes the current level of job growth is sufficient to keep downward pressure on the unemployment rate. In addition, wage growth is likely to be supported by employment gains and an unemployment rate hovering around the level of full employment.

As expected, given recent inflation data and the June increase in the targeted Federal Funds rate, the yield curve flattened considerably during the second quarter. As a result, longer duration bonds outperformed other fixed income segments with a return of 4.4%, as measured by the Bloomberg Barclays Long US Government/Credit Index.

4. Performance: Investment performance was positive for the quarter ended June 30, 2017. The system’s total assets returned 3.6% for the quarter, outperforming the Policy Index which returned 3.2%%. The System’s domestic stocks gained 3.2%, outperforming the S&P 1500 Stock

Index which returned 3.0% for the quarter. The System's international stocks were up 7.5%, besting the MSCI All Country ex US Index which had a return of 6.0% for the quarter. Alternatives and additional categories were positive contributors as Private Equity gained 4.8% while additional categories returned 1.3%. The System's bonds returned 1.6%, slightly underperforming the Barclays Gov/Credit Bond Index which returned 1.7% for the second quarter. Real Estate provided strong returns for the quarter gaining 2.0%.

Recommendation: The Executive Secretary recommends that the board accept and ratify the Report of the Investment Committee.

TOTAL BV INVESTED AT 3/31/17 \$ 14,495,277,098.16

April Activity

Purchases	727,783,387.76	
Disposals	(618,381,169.77)	
Paydowns	(4,941,725.73)	
Redemptions	(20,665,501.73)	
Short-Term Pool Net	<u>(19,759,060.71)</u>	64,035,929.82

May Activity

Purchases	502,478,827.01	
Disposals	(549,840,184.44)	
Paydowns	(1,830,929.65)	
Redemptions	(23,324,222.71)	
Short-Term Pool Net	<u>(65,435,198.07)</u>	(137,951,707.86)

June Activity

Purchases	621,923,146.52	
Disposals	(393,793,462.52)	
Paydowns	(2,007,433.32)	
Redemptions	(16,367,098.60)	
Short-Term Pool Net	<u>(15,340,215.93)</u>	194,414,936.15

TOTAL BV INVESTED AT 6/30/17 \$ 14,615,776,256.27

* TRS recognizes investment transactions on the date they occur. Transaction settlements, generally, occur days following transactions. The interim period between transaction date and settlement date represents a "pending period". At the time this statement was produced, (\$26,219,472.46) in net transactions had occurred but had not settled. The statement does not include either expected cash receipts or disbursements associated with these pending trades. Upon settlement of these pending transactions, the net effect would be as follows:

Total Short Term	545,314,302
- Pending Payable	<u>(26,219,472)</u>
Net	<u>519,094,830</u>

INVESTMENT ACTIVITY

April 1, 2017 -- June 30, 2017

Total Book Value Invested @ 4/1/17 \$ 14,495,277,098.16

Purchases:

411	Cash Equivalents	\$ 818,458,169.64	
155	Fixed Income Securities	712,840,567.13	
1289	Equity Securities	812,871,324.22	
27	Real Estate	55,793,612.39	
67	Alternative Investments	65,323,134.57	
139	Additional Categories	205,356,722.98	
2088	Total Purchases		\$ 2,670,643,530.93

Disposals:

334	Cash Equivalents	\$ 918,992,644.35	
88	Fixed Income Securities	483,162,114.58	
334	Principal Paydowns	8,780,088.70	
32	Redemptions / Maturities	52,381,438.41	
1830	Equity Securities	820,429,796.33	
32	Real Estate	16,453,523.07	
138	Alternative Investments	69,290,336.96	
129	Additional Categories	172,679,045.79	
0	Additional Principal Paydowns	-	
10	Additional Redemptions / Maturities	7,975,384.63	
2927	Total Disposals		\$ 2,550,144,372.82

Total Book Value Invested @ 6/30/17 \$ 14,615,776,256.27

Total Par Value Invested @ 6/30/17 \$ 14,597,912,045.61

Total Market Value Invested @ 6/30/17 \$ 18,617,890,295.13

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Total Short Term	545,314,302
- Pending Payable	(26,219,472)
Net	<u>519,094,830</u>

TO: Board of Trustees of the
Teachers' Retirement System of Kentucky

FROM: Gary L. Harbin, CPA
Executive Secretary

DATE: September 18, 2017

SUBJECT: Report of the Insurance Committee

The Insurance Committee will have a special meeting on September 18, 2017, prior to the regular quarterly meeting of the board. The committee will present a report to the board during the regular quarterly meeting.

TO: Board of Trustees
Teachers' Retirement System of Kentucky

FROM: Gary L. Harbin, CPA
Executive Secretary

DATE: September 18, 2017

SUBJECT: Report of the Insurance Committee

The Insurance Committee met prior to the regular quarterly meeting of the board on September 18, 2017. The Insurance Committee approved the following:

1. TRS MEHP 2018: The rate of \$258 per month for the TRS MEHP (combined United Healthcare Medicare Advantage and Express Scripts Medicare Part D) for those retirees fulfilling the necessary service requirements.

2. Know Your Rx Coalition: An additional fee of \$.25 PPPM paid to the Know Your Rx Coalition for additional medication therapy services within the pharmacogenomic pilot project with Coriell. This fee is effective as of July 1, 2017.

3. KEHP 2018:

- A medical insurance benefit supplement up to \$660.04 per month for those retirees fulfilling the necessary service requirements.
- Administrative Fee: \$7.44 PPPM for plan year 2018. (The state budget may increase the fee beginning in July 2018. Staff will report to the committee any increase in the administrative fee for plan year 2018.)

4. Non-single Subsidy for KEHP: A payment of the non-single subsidy to retirees under 65 who retired before July 1, 2010 for the first half of medical insurance plan year 2018 (Jan. 1, 2018 through June 30, 2018) and thereafter to continue the subsidy for the second half of the plan year 2018 (July 1, 2018 through Dec. 31, 2018) as authorized by the legislature and/or mandated by law.

Executive Secretary's Recommendation: The board should accept and ratify the actions of the Insurance Committee.

TO: Board of Trustees of the
Teachers' Retirement System of Kentucky

FROM: Gary L. Harbin, CPA
Executive Secretary

DATE: September 18, 2017

SUBJECT: Executive Secretary's Observations and Comments

1. Trustee Education Program: The Board of Trustees of TRS has always been devoted to gaining timely and relevant training on matters related to the proper administration of the retirement system. The board expressed its dedication to continuing education on November 17, 2008 when it adopted the Teachers' Retirement System Trustee Education Program in accordance with KRS 161.250(3)(c). Chapter 3, subparagraph 6 of the program provides that the executive secretary will report concerning this program each year at the September meeting of the board.

From July 2016 through June 2017, trustees attended more than 141 hours of combined approved training in accordance with the program. The approved training activities included a mix of programs and activities presented by national retirement associations, TRS staff and TRS service providers with particular expertise in investments, law and actuarial concepts. Topics covered a broad range of subjects including pension and medical benefits administration, investment concepts, legal compliance and fiduciary duty and other matters that enhance the effectiveness of trustees in fulfilling their role and satisfying their duties under law.

TRS staff has also assisted with providing specific training to trustees. TRS staff presented a one-day workshop in Frankfort that focused primarily on investment concepts, ethics and governance matters.

2. The November 2017 Trustee Workshop: TRS staff is planning a one-day trustee workshop in Frankfort that will focus on current issues in the administration of the retirement system. Staff anticipates presentations on funding, plan design, actuarial issues, investment concepts, ethics, governance and other matters. The trustee workshop has been scheduled tentatively for Monday, November 20, 2017.

3. Communications Consultant: In September 2009, the board approved retaining a communications consultant for assistance in presenting issues related to funding health care for retired teachers. The communications consultant was very helpful in developing messages for members and legislators concerning the very complex topic of retiree health care. In the coming year, the executive secretary anticipates that there will be a continuing need to use a communications consultant for issues related to retirement security and properly funding retirement benefits. In June 2017, the board approved the administrative budget for fiscal year 2017-2018 that included \$120,000 for hiring a communications consultant.

Recommendation: The executive secretary recommends that staff be authorized to renew the contract with the communications consultant for any needed services in the coming year.

4. GASB Statement Nos. 67 and 68: In June 2012, the GASB approved two statements concerning the accounting and financial reporting of pensions by state and local governments and pension plans. Statement No. 67, *Financial Reporting for Pension Plans*, addresses financial reporting for state and local government pension plans. Statement No. 68, *Accounting and Financial Reporting for Pensions*, establishes new accounting and financial reporting requirements for governments that provide their employees with pensions. While the two statements were being developed, TRS took an active role in communicating issues and concerns to GASB through a consortium of similarly situated public pension plans.

Statement No. 67 took effect for the fiscal year ending June 30, 2014. Statement No. 68 took effect for the state and universities for the fiscal year ending June 30, 2015.

There has been some concern as to how these new accounting standards apply to Kentucky school districts, particularly whether these new accounting standards would affect the budgets of the districts. In response, there are two important points to note.

Two Points Regarding the New Standards: First, as a critical reminder, GASB standards in general apply only to financial reporting. They do not mandate how a governmental pension plan is to be funded. In Kentucky, the commonwealth has a statutory obligation to provide pension funding through the employer retirement contributions it makes on behalf of teachers and administrators. As such, the responsibility for making employer contributions and addressing the unfunded liability of TRS rests with the commonwealth, not the local school districts. The new GASB accounting standards do not change the funding responsibility. GASB accounting standards do not require school districts to make employer contributions to TRS.

Second, it is true that the new GASB accounting standards do impose financial reporting standards on governmental employers regarding pension liability. However, Kentucky is very different from other states in the respect that Kentucky teachers and administrators are generally treated as employees of the Commonwealth for pension and other purposes. Given this circumstance, GASB has confirmed that the Commonwealth is responsible for reporting the annual required contributions and pension liabilities. Furthermore, GASB has also confirmed that Kentucky school districts will not be required to report a share of the pension liability in their financial statements.

TRS Reports: TRS published the accounting information required under Statement No. 67 in TRS's Comprehensive Annual Financial Report for the fiscal year ending June 30, 2016.

On June 23, 2017, TRS published the "GASB Statement No. 68 Report... Prepared as of June 30, 2016" for use by the state and universities. TRS's report was audited by the external auditor, which expressed the opinion that the schedules present fairly, in all material respects, the employer allocation and other matters addressed.

Recommendation: The GASB Statement No. 68 Report and the external audit report are available for review by the board.

5. Board of Trustees Governance Manual: The Board of Trustees Governance Manual was adopted on March 16, 2009. Since adoption, the manual has been amended and updated several times. Staff is recommending amendments detailed below to conform to changes to state law and accounting standards. Appendices 16, 17 and 18 with proposed amendments are attached.

- Appendix 16 “Charter of the Governance and Audit Committee” should be amended to provide for the committee accepting the reports of the annual audit and the annual actuarial valuations on behalf of the Board of Trustees. (See paragraph 5(H)) This amendment accommodates SB 2 (RS 2017), which mandates delivering the reports to the Public Pension Oversight Board by November 15 each year.
- Appendix 17 “Policies on Annual Retirement Appropriations Payable by the State, Retiree Medical Plan and Life Insurance Plan” should be amended to include funding principles for the retiree medical plan and life insurance plan consistent with GASB Statement Nos. 74 and 75. GASB Statement No. 74 will be implemented with the fiscal year 2017 valuation of the retiree medical and life insurance plans. GASB Statement No. 75 will be implemented and reported in June 2018.
- Appendix 18 “Procurement Procedures” should be amended to conform to SB 2 (RS 2017) requiring procurements of goods and services be subject to KRS Chapters 45, 45A, 56 and 57. TRS staff met with the Secretary of the Finance and Administration Cabinet on August 8, 2017. The secretary recommended that the Board of Trustees establish small purchase authority limits for TRS staff. The executive secretary recommends staff be authorized to make small purchases up to \$20,000 consistent with the Appendix 18 Procurement Procedures and applicable state law.

Recommendation: The Executive Secretary recommends that the proposed amendments to Appendices 16, 17 and 18 be approved.

6. Executive Secretary’s Meetings: The executive secretary has had meetings with several groups recently and will report to the board concerning the following:

June 20, 2017	Meeting with public relations consultant
June 28, 2017	Meeting with KRTA representatives
June 29, 2017	Meeting with Tom Loftus, Louisville Courier Journal
June 29, 2017	Meeting with investment manager
July 11, 2017	Conference call with actuaries
July 13, 2017	Conference call with investment manager
July 18, 2017	Orientation for new trustee
July 19, 2017	Orientation for new trustee
July 20, 2017	Conference call with investment consultant and actuary

July 26, 2017	Presentation to KEDC
July 27, 2017	Presentation to KASA
July 31, 2017	Meeting with Representative Reed and Chair Sanders
August 1, 2017	Meeting with representatives from Fort Washington Investment Advisors
August 3, 2017	Meeting with new KRTA executive director
August 8, 2017	Meeting with Secretary of Finance and Administration Cabinet
August 9, 2017	Meeting with public relations consultant
August 11, 2017	Conference call with actuaries
August 18, 2017	Meeting with KEA representatives
August 21, 2017	Conference call with investment experts
August 21, 2017	Meeting with public relations consultant
August 25, 2017	Presentation to KRTA Fall Workshop Jefferson County
August 26, 2017	Meeting with KEA representatives
August 30, 2017	Meeting with public relations consultant
September 1, 2017	Meeting with Todd Asset Management
September 5, 2017	Know Your RX Coalition Board meeting
September 14, 2017	Attended District 4 KRTA Fall Workshop

7. Next Meeting: The next quarterly meeting of the board will be December 18, 2017.

BOARD GOVERNANCE MANUAL

APPENDIX 16 CHARTER OF THE GOVERNANCE AND AUDIT COMMITTEE

1. Purpose

The Governance and Audit Committee is a committee of the Board of Trustees of the Teachers' Retirement System of the State of Kentucky (TRS). The committee is established to assist the Board of Trustees in fulfilling its fiduciary oversight responsibilities for TRS's governance process, financial reporting process, system of risk management, system of internal control, internal and external audit process and the process of monitoring compliance with laws and regulations.

2. Authority

The committee has authority for matters within its scope of responsibility for the following functions:

- A. Governance process;
- B. Financial reporting process;
- C. System of risk management;
- D. System of internal controls;
- E. Internal and external audit;
- F. Monitoring compliance with laws and regulations; and
- G. Audit management and reporting.

3. Composition

The committee will consist of a minimum of three trustees appointed by the board chair. The board chair should endeavor to appoint at least one member with an understanding of generally accepted accounting principles and financial statements; experience in the preparation or auditing of financial statements; experience with internal accounting controls; and an understanding of audit committee functions.

4. Meetings

The committee will not have regular meetings, but will meet at least twice each year (to review the external audit report and to review the internal audit plan) and may convene for additional meetings as circumstances require. All committee members are expected to attend each meeting. The committee will invite members of management, auditors and/or others to attend meetings and provide pertinent information as necessary. Subject to open meetings laws, the committee may meet in executive session. Meeting agendas will be prepared and provided in advance to members, along with appropriate briefing materials. Minutes of each meeting will be prepared.

5. Responsibilities

The committee will have responsibility for providing policy recommendations to the Board of Trustees regarding:

- A. Assessing of governance processes;
- B. Assuring the integrity of financial information reporting;
- C. Policies and frameworks for an effective system of risk management and the mechanisms for periodic assessment of the system of risk management;
- D. Assessing internal administrative and accounting controls by both the external and internal auditors;
- E. Policies and frameworks for an effective system of internal controls and the mechanisms for periodic assessment of the system of internal controls;
- F. Reviewing with management and the director of internal audit the objectives, plans, activities, staffing and organizational structure of the internal audit function;
- G. Reviewing the effectiveness of the system of monitoring and compliance with applicable statutes, regulations and policies;
- H. Accept the reports of the annual audit of the financial statements and the annual actuarial valuations on behalf of the Board of Trustees; and
- I. Reporting to the Board of Trustees on significant activities, findings and recommendations of the committee.

Adopted August 28 2009; amended September 19, 2016 and September 18, 2017

BOARD GOVERNANCE MANUAL

APPENDIX 17

POLICIES ON ANNUAL RETIREMENT APPROPRIATIONS PAYABLE BY THE STATE, RETIREE MEDICAL PLAN AND LIFE INSURANCE PLAN

INTRODUCTION

Pursuant to the provisions of KRS 161.250, the Board of Trustees (board) of the Teachers' Retirement System of the State of Kentucky (TRS) is vested with the responsibility for the general administration and management of the retirement system. The board may adopt procedures necessary to conduct the business of the retirement system as needed. The applicable provisions of the Kentucky Revised Statutes shall control if any inconsistency exists between state law and this policy.

1. Retirement Appropriations

State law provides that the retirement benefits promised to members of TRS are "an inviolable contract of the Commonwealth ... (KRS 161.714)." To satisfy this solemn commitment, the Commonwealth of Kentucky (state) is required to pay annual retirement appropriations necessary to fund the benefit requirements of retirement system members. All employers participating in TRS are responsible for paying the fixed employer contribution rate set forth in state law. However, the state – as plan guarantor – is solely responsible for paying the additional annual retirement appropriations necessary to keep the retirement system actuarially sound and able to satisfy the contract with members to provide promised benefits (KRS 161.550 (6)).

Since fiscal year 2008, the state has not paid the full recommended annual retirement appropriations necessary to prefund the benefit requirements of members of the retirement system as determined by the actuary. Over this period, because of the failure to fund, the state's annual retirement appropriations have grown significantly from \$60.5 million (Fiscal Year 2009) to \$487.4 million (Fiscal Year 2016). The following schedule details the growth of the annual retirement appropriations payable by the state:

Fiscal Year	Cumulative Increase as a % of Payroll	Cumulative Increase of Annual Retirement Appropriations Payable by the State
2009	1.88	\$ 60,499,800
2010	2.46	82,331,200
2011	3.59	121,457,000
2012	5.81	208,649,000
2013	7.27	260,980,000
2014	8.02	299,420,000
2015	10.42	386,400,000
2016	12.97	487,400,000
2017	13.80	520,372,000
2018	13.49	512,883,000
2019	14.61	553,597,000

(Source: TRS Report of the Actuary on the Annual Valuation Prepared as of June 30, 2016)

The board always has acted as required by state law and recommended annual retirement appropriations payable by the state that would ensure that the state meets the contractual obligations to members. This policy confirms the board's process for recommending annual retirement appropriations payable by the state and the primary actuarial assumptions and methodologies associated with calculating the annual retirement appropriations. Other related actuarial assumptions and methodologies not listed in this policy are reported in annual valuations, the most recent experience study or resolutions adopted by the board.

Annual Retirement Appropriations Payable by the State

In each biennial budget request, the board will recommend annual retirement appropriations payable by the state to meet the benefit requirements of the members of the retirement system. The annual retirement appropriations payable by the state are the sum of the fixed employer contribution rate set by state law and the additional annual retirement appropriations necessary to fund the benefit requirements of members of the retirement system (KRS 161.550). The recommended additional annual retirement appropriations payable by the state are calculated by the board's actuary based upon the results of an annual valuation preceding the beginning of each biennium (KRS 161.400).

Calculation of Annual Retirement Appropriations Payable by the State

The board will recommend annual retirement appropriations payable by the state, which if paid, will meet the benefit requirements of the members of the retirement system, consistent with generally accepted actuarial principles. Based upon technical advice from the board's actuary, the board hereby adopts the following principles for calculating the recommended annual retirement appropriations payable by the state:

- A. Use the Entry Age Normal actuarial cost method;
- B. Use a five-year asset smoothing method;
- C. Use a 30-year closed period to amortize, as a level percentage of pay, legacy unfunded liability (legacy unfunded liability is that unfunded liability recognized as of the valuation prepared for June 30, 2014);
- D. Use a 20-year closed period to amortize, as a level percentage of pay, new sources of unfunded liability (new sources of unfunded liability are the unfunded liability consisting of all benefit changes, assumption and method changes and experience gains and/or losses that have occurred since the previous valuation); and
- E. Reach a minimum funding ratio of 100 percent within the 30-year closed amortization period.

The board also recognizes that the state may desire to contribute lump sum payments toward satisfaction of unfunded liability rather than amortization of the debt. Total unfunded liability is published in every annual valuation of the retirement system, and TRS will work with the state to develop reasonable and appropriate plans for receipt of lump sum payments toward the satisfaction of unfunded liability.

2. Retiree Medical Plan

State law provides for a retiree medical plan (KRS 161.675). Since July 1, 2010, retired teachers, active teachers, local school boards, universities and the state have paid contributions for funding the retiree medical plan in accordance with the “Shared Responsibility Solution” (HB 540, RS 2010). The contributions mandated by Shared Responsibility will meet the benefit requirements of the members of the retirement system, consistent with generally accepted actuarial principles. Based upon technical advice from the board’s actuary, the board hereby adopts the following principles concerning the retiree medical plan:

- A. Use the Entry Age Normal actuarial cost method;
- B. Use a five-year asset smoothing method;
- C. Use a 30-year closed period to amortize, as a level percentage of pay, legacy unfunded liability (legacy unfunded liability is that unfunded liability recognized as of the valuation prepared for June 30, 2017);
- D. Use a 20-year closed period to amortize, as a level percentage of pay, new sources of unfunded liability (new sources of unfunded liability are the unfunded liability consisting of all benefit changes, assumption and method changes and experience gains and/or losses that have occurred since the previous valuation); and
- E. Reach a minimum funded ratio of 100 percent within the 30-year closed amortization period.

This policy also confirms the primary actuarial assumptions and methodologies associated with the retiree medical plan. Other related actuarial assumptions and methodologies not listed in this policy are reported in annual valuations, the most recent experience study or resolutions adopted by the board.

3. Life Insurance Plan

State law provides for a life insurance plan for active and retired teachers (KRS 161.655). The life insurance plan is funded by employer contributions. Based upon technical advice from the board’s actuary, the board hereby adopts the following principles concerning the life insurance plan:

- A. Use the Entry Age Normal actuarial cost method;
- B. Use a five-year asset smoothing method;
- C. Use a 30-year closed period to amortize, as a level percentage of pay, legacy unfunded liability (legacy unfunded liability is that unfunded liability recognized as of the valuation prepared for June 30, 2017);
- D. Use a 20-year closed period to amortize, as a level percentage of pay, new sources of unfunded liability (new sources of unfunded liability are the unfunded liability consisting of all benefit changes, assumption and method changes and experience gains and/or losses that have occurred since the previous valuation); and

- E. Reach a minimum funded ratio of 100 percent within the 30-year closed amortization period.

This policy also confirms the primary actuarial assumptions and methodologies associated with the life insurance plan. Other related actuarial assumptions and methodologies not listed in this policy are reported in annual valuations, the most recent experience study or resolutions adopted by the board.

This policy will be reviewed regularly and amended or revised as necessary.

DRAFT

Adopted December 16, 2013; amended December 9, 2015; September 19, 2016, September 18, 2017

BOARD GOVERNANCE MANUAL

APPENDIX 18 PROCUREMENT PROCEDURES

1. Adoption of Procurement Procedures

Pursuant to the provisions of KRS 161.250, the Board of Trustees (board) of the Teachers' Retirement System of the State of Kentucky (TRS) is vested with the responsibility for the general administration and management of the retirement system. The board may adopt procedures necessary to conduct the business of the retirement system as needed. The law shall control if any inconsistency exists between the law and these procurement procedures.

2. Law

KRS 161.330 provides that the board is responsible for the approval and administration of expenses for the operation of the retirement system, and the board is authorized to purchase or lease suitable office quarters for the operation of the retirement system. Additionally, KRS 161.340 (3) provides that the board is responsible for the contracting of commodities (goods); actuarial, auditing, legal, medical and investment counseling; and other professional or technical services as are required to carry out the obligations of the board, subject to KRS Chapters 45, 45A, 56 and 57.

3. Goods and Services

For each fiscal year, the board approves an administrative budget for anticipated goods and services required to carry out the obligations of the board. The board authorizes staff to procure goods and services by competitive sealed bidding, competitive negotiation, noncompetitive negotiation or small purchase procedures. All payments on contracts for goods and services are issued only on written authorization of the executive secretary or a deputy executive secretary. Thereafter, staff issues a report to the board comparing actual to budgeted expenditures.

4. Small Purchases

The board authorizes staff to procure goods or services for small purchases as follows:

- A. Procurement of goods and services costing equal to or less than \$5,000 during any one fiscal year requires at least one quote. Quotes may be obtained by telephone, email, fax or by posting a solicitation to an e-procurement website of the Commonwealth. TRS will maintain a file documenting the quote(s) received and the award.
- B. Procurement of goods and services costing more than \$5,000 and equal to or less than \$20,000 during any one fiscal year requires a minimum of three quotes. Quotes may be obtained by telephone, email, fax or by posting a solicitation to an e-procurement website of the Commonwealth. TRS will maintain a file documenting the quotes received and the award.

5. Other Laws and Policies that Comprise TRS Procurement Procedures

The foregoing procurement procedures are to be implemented in conjunction with, and accordance to, the laws and other policies that, cumulatively, establish the comprehensive TRS procurement policy by which all TRS procurements are made. These laws and other policies include:

- A. Board Governance Manual, Section 8 – Service Provider Selection;
- B. Board Governance Manual, Appendix 7 – Conflict of Interest and Confidentiality Policy, External Service Provider Conflict of Interest Statement, Board of Trustees and Employees Conflict of Interest Statement;
- C. TRS Conflict of Interest Contract Language;
- D. Cost of Administration, how paid (KRS 161.330);
- E. Contracting for Services (KRS 161.340 (3));
- F. Board to act as fiduciary in ensuring that assets are used to pay benefits and expenses are defrayed (KRS 161.420);
- G. Investment Requirements (KRS 161.430), (102 KAR 1:175);
- H. TRS Investment Procurement Policy;
- I. Executive Branch Code of Ethics (KRS 11A);
- J. TRS Conflict of Interest Prohibitions (KRS 161.460);
- K. TRS Confidentiality requirement (KRS 161.585);
- L. TRS Insurance Fund (KRS 161.677); and
- M. Investment Policies for TRS Insurance Fund (102 KAR 1:178).

Adopted June 15, 2015; amended: September 19, 2016, November 21, 2016 and September 18, 2017