TEACHERS' RETIREMENT SYSTEM OF THE STATE OF KENTUCKY

Financial Statements

June 30, 2012

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Mountjoy
Chilton
Medley

Independent Auditor's Report on Financial Statements

To the Board of Trustees
Teachers' Retirement System of the State of Kentucky
Frankfort, Kentucky

We have audited the accompanying statement of plan net assets of the Teachers' Retirement System of the State of Kentucky as of and for the year ended June 30, 2012, and the related statement of changes in plan net assets for the year then ended. These component unit financial statements are the responsibility of the Teachers' Retirement System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the Teachers' Retirement System of the State of Kentucky, a component entity of the Commonwealth of Kentucky, as of June 30, 2012, and the respective changes in its plan net assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The financial statements of Teachers' Retirement System of the State of Kentucky as of June 30, 2011, were audited by other auditors whose report dated December 16, 2011 expressed an unmodified opinion on those statements.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 17, 2012, on our consideration of the Teachers' Retirement System of the State of Kentucky's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Teachers' Retirement System of the State of Kentucky's financial statements as a whole. The financial section and supporting schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements. These schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Mountjoy Chilton Medley LLP

Lexington, Kentucky
December 17, 2012

TEACHERS' RETIREMENT SYSTEM OF THE STATE OF KENTUCKY
MANAGEMENT'S DISCUSSION AND ANALYSIS

This discussion and analysis of The Teachers' Retirement System of the State of Kentucky (Kentucky Teachers' Retirement System, KTRS, System, or Plan) financial performance provides an overview of the defined benefit and medical insurance plans' financial year ended June 30, 2012. Please read it in conjunction with the respective financial statements, which begin on page 8.

USING THIS FINANCIAL REPORT

Because of the long-term nature of the defined benefit retirement annuity plan, and the medical and life insurance plans, financial statements alone cannot provide sufficient information to properly reflect the ongoing perspective of the System. The Statement of Plan Net Assets and Statement of Changes in Plan Net Assets (on pages 8-11) provide information about the activities of the defined benefit retirement annuity plan, medical insurance plan, life insurance plan and the tax-sheltered annuity plan as a whole. The Kentucky Teachers' Retirement System is the fiduciary of funds held in trust for its members.

The Schedule of Funding Progress (on pages 33-35) includes historical trend information about the actuarially funded status of each plan from a long-term, ongoing plan perspective and the progress made in accumulating sufficient assets to pay benefits and insurance premiums when due. The Schedule of Employer Contributions (on pages 33-35) presents historical trend information about the annual required contributions of employers and the contributions made by employers in relation to the requirement. These schedules provide information that contributes to understanding the changes over time in the funded status of the plans.

KENTUCKY TEACHERS' RETIREMENT SYSTEM AS A WHOLE

In the fiscal year ended June 30, 2012, Kentucky Teachers' Retirement System's combined plan net assets decreased by $285.8 million – from $15,514.9 million in 2011 to $15,229.1 million in 2012. In 2010, combined net assets totaled $12,786.7 million. The following summaries focus on plan net assets and changes in plan net assets of Kentucky Teachers' Retirement System's defined benefit retirement annuity plan, medical insurance plan, life insurance plan and other funds.

Summary of Plan Net Assets
(In Millions)

	Defined Benefit Plan			Medical Insurance Plan			Life Insurance Fund		
Categories	2012	2011	2010	2012	2011	2010	2012	2011	2010
Cash & Investments	$ 15,123.6	$ 15,192.9	$ 12,513.9	$ 345.0	$ 429.2	$ 237.1	$ 91.1	$ 87.4	$ 87.1
Receivables	133.4	180.7	96.5	16.3	5.3	7.9	1.1	1.1	0.9
Capital Assets	6.8	3.8	3.4	-	-	-	-	-	-
Total Assets	15,263.8	15,377.4	12,613.8	361.3	434.5	245.0	92.2	88.5	88.0
Total Liabilities	(466.7)	(246.8)	(157.2)	(22.5)	(139.7)	(3.8)	-	-	(0.1)
Plan Net Assets	$ 14,797.1	$ 15,130.6	$ 12,456.6	$ 338.8	$ 294.8	$ 241.2	$ 92.2	$ 88.5	$ 87.9

*Totals	2012	2011	2010
Cash & Investments	$ 15,559.7	$ 15,709.5	$ 12,838.1
Receivables	150.8	187.1	105.3
Capital Assets	6.8	3.8	3.4
Total Assets	$ 15,717.3	15,900.4	12,946.8
Total Liabilities	(489.2)	(386.5)	(161.1)
Plan Net Assets	$ 15,228.1	$ 15,513.9	$ 12,785.7

**Other Funds consisting of the 403(b) Tax Shelter Plan, the Excess Benefit Fund and the Losey Scholarship fund had combined plan net assets of $.9 million for years ended 2012, 2011 and 2010.*

Plan net assets of the defined benefit retirement annuity plan decreased by 2.2% ($14,797.1 million compared to $15,130.6 million) and in 2010, plan net assets of the defined benefit plan totaled $12,456.6 million. The decrease is primarily due to unfavorable market conditions which resulted in a net investment income decrease of $2.45 billion less than 2011. The 2012 amount was $1.2 billion less than 2010. The defined benefit retirement annuity plan assets are restricted to providing monthly retirement allowances to members and their beneficiaries. Plan net assets of the medical insurance plan increased by 14.9% ($338.8 million compared to $294.8 million) primarily due to contributions from members and employers exceeding insurance expenses due to legislation passed in 2010. This compares to 2010 where plan net assets of the medical insurance fund totaled $241.2 million. Plan assets are restricted to providing hospital and medical insurance benefits to members and their spouses.

Summary of Changes in Plan Net Assets (In Millions)

	Defined Benefit Plan			Medical Insurance Plan			Life Insurance Fund		
Categories	2012	2011	2010	2012	2011	2010	2012	2011	2010
Additions									
Member Contributions	$ 309.8	$ 302.3	$ 297.6	$ 100.3	$ 84.1	$ 63.8	$ -	$ -	$ -
Employer Contributions	557.3	1,037.9	479.8	174.0	188.3	158.8	1.7	1.7	1.9
Net Investment Income (loss)	309.7	2,761.0	1,509.8	(4.0)	8.3	12.3	6.4	3.1	5.4
Other Income	-	-	-	3.8	0.5	14.6	-	-	-
Total Additions	$ 1,176.8	$ 4,101.2	$ 2,287.2	$ 274.1	$ 281.2	$ 249.5	$ 8.1	$ 4.8	$ 7.3
Deductions									
Benefit Payments	$ 1,482.9	$ 1,402.6	$ 1,321.8	$ -	$ -	$ -	$ 4.4	$ 4.2	$ 4.1
Refunds	19.5	17.3	15.3	-	-	-	-	-	-
Administrative Expense	7.8	7.3	8.8	1.2	1.2	-	-	-	-
Insurance Expenses	-	-	-	229.0	226.4	237.4	-	-	-
Total Deductions	1,510.2	1,427.2	1,345.9	230.2	227.6	237.4	4.4	4.2	4.1
Increase/(Decrease) in Plan Net Assets	$ (333.4)	$ 2,674.0	$ 941.3	$ 43.9	$ 53.6	$ 12.1	$ 3.7	$ 0.6	$ 3.2

*Totals	2012	2011	2010
Additions			
Member Contributions	$ 410.1	$ 386.4	$ 361.4
Employer Contributions	733.0	1,227.9	640.5
Net Investment Income	312.1	2,772.4	1,527.5
Other Income	3.8	0.5	14.6
Total Additions	$ 1,459.0	$ 4,387.2	$ 2,544.0
Deductions			
Benefit Payments	$ 1,487.3	$ 1,406.8	$ 1,325.9
Refunds	19.5	17.3	15.3
Administrative Expense	9.0	8.5	8.8
Insurance Expenses	229.0	226.4	237.4
Total Deductions	$ 1,744.8	$ 1,659.0	$ 1,587.4
Increase/(Decrease) in Plan Net Assets	$ (285.8)	$ 2,728.2	$ 956.6

DEFINED BENEFIT RETIREMENT ANNUITY PLAN ACTIVITIES

Member contributions increased $7.5 million. Retirement contributions are calculated by applying a percentage factor to salary and are paid monthly by each member. Members may also pay contributions to repurchase previously refunded service credit or to purchase various types of elective service credit.

Employer contributions totaled $557.3 million, a net decrease of $480.6 million from the 2011 fiscal year. This was primarily due to bond proceeds received in the 2011 fiscal year of $465.4 million to satisfy amounts that were being amortized in the state budget. These bond proceeds, along with $124.3 million of contributions redirected to the medical insurance fund from the pension fund caused the employer contributions to be $558.1 million more in 2011 when compared to 2010.

The System experienced a decrease in net investment income compared to the previous year ($309.7 million at June 30, 2012 as compared to a $2,761.0 million at June 30, 2011). For 2010, net investment income totaled $1,509.8 million. The decrease in the fair value of investments is mainly due to unfavorable market conditions for the year ended June 30, 2012 and is illustrated as follows:

(In Millions)	2012	2011	2010
Appreciation(depreciation) in fair value of investments - June 30, prior year	$ 1,842.0	$ (235.5)	$ (1,336.2)
Appreciation(depreciation) in fair value of investments - June 30, end of year	1,411.6	1,842.0	(235.5)
Change in net appreciation(depreciation) in fair value of investments	(430.4)	2,077.5	1,100.7
Net income (net of investment expense)	378.2	362.3	341.3
Net gain on sale of investments	361.9	321.2	67.8
Investment Income (net) - June 30, end of year	$ 309.7	$ 2,761.0	$ 1,509.8

Program deductions in 2012 increased $83.0 million. The increase was caused principally by an increase of $80.3 million in benefit payments. Members who were drawing benefits as of June 2011 received an increase of 1.5% to their retirement allowances in July 2011. Also, there was an increase of 1,675 members and beneficiaries on the retired payroll as of June 30, 2012.

OTHER POST EMPLOYMENT BENEFIT ACTIVITIES

During the 2012 fiscal year, the medical insurance plan member contributions increased $16.2 million and employer contributions decreased $14.3 million under fiscal year 2011. The member contributions increased primarily due to the implementation of the Shared Responsibility Plan beginning July 1, 2010 which includes increased contributions from active and retired members, employers and the state. The employer contributions decreased due to less transition funding paid by the state as the Shared Responsibility plan phases in until the 2016 fiscal year. The state's contribution for the 2010-2012 biennium was made with bond proceeds received in March 2011.

Net investment income decreased $12.3 million from $8.3 million in 2011 to a negative $4.0 million in 2012. In 2010, net investment income totaled $12.3 million. This can be illustrated as follows:

(In Millions)	2012	2011	2010
Appreciation(depreciation) in fair value of investments - June 30, prior year	$ -	$ -	$ -
Appreciation(depreciation) in fair value of investments - June 30, end of year	(9.7)	-	-
Change in net appreciation(depreciation) in fair value of investments	(9.7)	-	-
Net income (net of investment expense)	6.0	8.3	12.3
Net gain (loss) on sale of investments	(0.3)	-	-
Investment Income (net) - June 30, end of year	$ (4.0)	$ 8.3	$ 12.3

The life insurance plan has an actuarial valuation conducted independently from the defined benefit plan. Total life insurance benefits paid for 2012, 2011 and 2010 were $4.4, $4.2, and $4.1 million respectively.

HISTORICAL TRENDS

Accounting standards require that the Statement of Plan Net Assets state asset value at fair value and include only benefits and refunds due plan members and beneficiaries and accrued investment and administrative expenses as of the reporting date. Information regarding the actuarial funding status of the defined benefit plan, the medical insurance plan, and the life insurance plan is provided in the Schedule of Funding Progress (beginning on page 33). The asset value, stated in the Schedule of Funding Progress, is determined by the System's independent actuary. The actuarial accrued liability is calculated using the entry age cost method.

The 2012 fiscal year reveals a decline in funding position of the retirement annuity plan due primarily to an increase in the actuarial liability while the actuarial value of the assets remained flat due to market decline in prior years. Annual required employer contributions of the defined benefit plan are provided in the Schedule of Employer Contributions (on page 33) and a shortfall of employer contributions has resulted in an accumulated net pension obligation of $436,123,560 as of June 30, 2012.

Although the medical insurance plan continues to have a large unfunded actuarial liability, the current obligations are being met by current funding. Effective July 1, 2010 the Shared Responsibility Plan for funding retiree health benefits requires members, retirees, participating employers and the state to make contributions for pre-funding retiree medical benefits. Annual required contributions of the medical insurance plan are provided in the Schedule of Employer Contributions (on page 34) and a shortfall of employer contributions has resulted in an accumulated net OPEB obligation of $1,413,736,073 as of June 30, 2012.

Teachers' Retirement System of the State of Kentucky
Statement of Plan Net Assets
as of June 30, 2012

	Defined Benefit Plan	Medical Insurance Plan	Life Insurance Plan	Other Funds	Total
Assets					
Cash	$ 25,314,512	$ 5,202,577	$ 299,153	$ 9,828	$ 30,826,070
Prepaid Expenses	62,774	147,000	-	-	209,774
Receivables					
Contributions	37,851,376	5,574,370	31,987	-	43,457,733
Due from Other Trust Funds	2,432,980	-	-	-	2,432,980
State of Kentucky	9,162,962	5,714,136	21,590	-	14,898,688
Investment Income	49,846,104	1,143,178	1,065,552	1,183	52,056,017
Investment Sales Receivable	33,559,535	-	-	-	33,559,535
Other Receivables	499,433	3,873,520	-	-	4,372,953
Total Receivables	133,352,390	16,305,204	1,119,129	1,183	150,777,906
Investments at Fair Value (See Note 5)					
Short Term Investments	608,260,247	57,658,400	4,521,129	673,015	671,112,791
Bonds and Mortgages	3,481,878,618	140,165,798	86,346,232	270,532	3,708,661,180
Equities	9,260,311,630	141,013,192	-	-	9,401,324,822
Alternative Investments	764,469,456	748,103	-	-	765,217,559
Real Estate	586,800,766	-	-	-	586,800,766
Total Investments	14,701,720,717	339,585,493	90,867,361	943,547	15,133,117,118
Invested Security Lending Collateral	396,546,893	-	-	-	396,546,893
Capital Assets, at Cost Net Of Accumulated Depreciation of $2,202,905 (See Note 2)	6,858,662	-	-	-	6,858,662
Total Assets	15,263,855,948	361,240,274	92,285,643	954,558	15,718,336,423
Liabilities					
Accounts Payable	4,052,099	3,762,868	-	-	7,814,967
Due To Other Trust Funds	-	2,387,658	44,397	925	2,432,980
Insurance Claims Payable	-	67,000	-	-	67,000
Revenues Collected in Advance	-	6,153,310	-	-	6,153,310
Investment Purchases Payable	66,136,067	10,122,885	-	-	76,258,952
Obligations Under Security Lending	396,546,893	-	-	-	396,546,893
Total Liabilities	466,735,059	22,493,721	44,397	925	489,274,102
Net Assets Held In Trust For Pension And Other Post Employment Benefits	$ 14,797,120,889	$ 338,746,553	$ 92,241,246	$ 953,633	$ 15,229,062,321

The "Schedule of Funding Progress" is presented in the Required Supplementary Information section of this report.
The accompanying notes are an integral part of these financial statements.

Teachers' Retirement System of the State of Kentucky
Statement of Plan Net Assets
as of June 30, 2011

	Defined Benefit Plan	Medical Insurance Plan	Life Insurance Plan	Other Funds	Total
Assets					
Cash	$ 2,014,331	$ 175,762	$ 385,672	$ 65,108	$ 2,640,873
Prepaid Expenses	40,263	147,000	-	-	187,263
Receivables					
Contributions	30,046,110	3,298,187	27,501	-	33,371,798
Due from Other Trust Funds	1,207,985	-	-	-	1,207,985
State of Kentucky	-	193,954	-	-	193,954
Investment Income	53,218,525	943,333	1,113,843	1,149	55,276,850
Investment Sales Receivable	95,747,740	-	-	-	95,747,740
Other Receivables	431,187	849,412	-	-	1,280,599
Total Receivables	180,651,547	5,284,886	1,141,344	1,149	187,078,926
Investments at Fair Value (See Note 5)					
Short Term Investments	588,462,274	141,587,315	1,654,850	698,978	732,403,417
Bonds and Mortgages	3,797,591,983	136,110,938	85,366,325	205,312	4,019,274,558
Equities	9,588,077,134	151,170,232	-	-	9,739,247,366
Alternative Investments	576,527,803	-	-	-	576,527,803
Real Estate	480,447,237	-	-	-	480,447,237
Total Investments	15,031,106,431	428,868,485	87,021,175	904,290	15,547,900,381
Invested Security Lending Collateral	159,808,327	-	-	-	159,808,327
Capital Assets, at Cost Net Of Accumulated Depreciation of $2,101,508 (See Note 2)	3,803,072	-	-	-	3,803,072
Total Assets	15,377,423,971	434,476,133	88,548,191	970,547	15,901,418,842
Liabilities					
Accounts Payable	1,221,191	-	-	-	1,221,191
Due To Other Trust Funds	-	1,186,029	21,511	445	1,207,985
Insurance Claims Payable	-	403,000	-	-	403,000
Revenues Collected in Advance	-	122,500,000	-	-	122,500,000
Investment Purchases Payable	85,788,174	15,568,509	-	-	101,356,683
Obligations Under Security Lending	159,808,327	-	-	-	159,808,327
Total Liabilities	246,817,692	139,657,538	21,511	445	386,497,186
Net Assets Held In Trust For Pension And Other Post Employment Benefits	$ 15,130,606,279	$ 294,818,595	$ 88,526,680	$ 970,102	$ 15,514,921,656

The "Schedule of Funding Progress" is presented in the Required Supplementary Information section of this report.
The accompanying notes are an integral part of these financial statements.

Teachers' Retirement System of the State of Kentucky
Statement of Changes in Plan Net Assets
For the Year Ended June 30, 2012

	Defined Benefit Plan	Medical Insurance Plan	Life Insurance Plan	Other Funds	Total
Additions					
Contributions					
Employer	$ 557,339,552	$ 173,966,623	$ 1,684,711	$ -	$ 732,990,886
Member	309,729,924	100,346,070	-	-	410,075,994
Total Contributions	867,069,476	274,312,693	1,684,711	-	1,143,066,880
Other Income					
Recovery Income	-	3,483,583	-	-	3,483,583
Medicare D Receipts	-	297,639	-	-	297,639
Total Other Income	-	3,781,222	-	-	3,781,222
Investment Income					
Net Appreciation/(Depreciation) in Fair Value of Investments	(68,546,089)	(9,970,177)	2,703,508	66,220	(75,746,538)
Interest	210,189,576	6,231,117	3,746,222	10,023	220,176,938
Dividends	163,431,233	32,266	-	-	163,463,499
Rental Income, Net	30,536,687	-	-	-	30,536,687
Securities Lending, Gross Earnings	3,104,925	-	292	-	3,105,217
Gross Investment Income	338,716,332	(3,706,794)	6,450,022	76,243	341,535,803
Less: Investment Expense	(28,088,560)	(282,408)	-	-	(28,370,968)
Less: Securities Lending Expense	(931,520)	-	-	-	(931,520)
Net Investment Income	309,696,252	(3,989,202)	6,450,022	76,243	312,233,315
Total Additions	1,176,765,728	274,104,713	8,134,733	76,243	1,459,081,417
Deductions					
Benefits	1,482,939,165	-	4,397,281	92,232	1,487,428,678
Refunds of Contributions	19,549,073	-	-	-	19,549,073
Insurance Expenses	-	228,975,126	-	-	228,975,126
Administrative Expense	7,762,880	1,201,629	22,886	480	8,987,875
Total Deductions	1,510,251,118	230,176,755	4,420,167	92,712	1,744,940,752
Net Increase(Decrease)	(333,485,390)	43,927,958	3,714,566	(16,469)	(285,859,335)
Net Assets Held In Trust For Pension And Other Postemployment Benefits					
Beginning of Year	15,130,606,279	294,818,595	88,526,680	970,102	15,514,921,656
End of Year	$ 14,797,120,889	$ 338,746,553	$ 92,241,246	$ 953,633	$ 15,229,062,321

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

Teachers' Retirement System of the State of Kentucky
Statement of Changes in Plan Net Assets
For the Year Ended June 30, 2011

	Defined Benefit Plan	Medical Insurance Plan	Life Insurance Plan	Other Funds	Total
Additions					
Contributions					
Employer	$ 1,037,935,993	$ 188,241,202	$ 1,668,822	$ 60,000	$ 1,227,906,017
Member	302,262,819	84,147,337	-	-	386,410,156
Total Contributions	1,340,198,812	272,388,539	1,668,822	60,000	1,614,316,173
Other Income					
Recovery Income	-	212,727	-	-	212,727
Medicare D Receipts	-	280,585	-	-	280,585
Total Other Income	-	493,312	-	-	493,312
Investment Income					
Net Appreciation/(Depreciation) in					
Fair Value of Investments	2,398,629,230	(200,122)	(691,253)	(5,937)	2,397,731,918
Interest	200,003,244	8,577,058	3,786,029	15,626	212,381,957
Dividends	152,176,305	18,438	-	-	152,194,743
Rental Income, Net	30,610,988	-	-	-	30,610,988
Securities Lending, Gross Earnings	2,447,181	-	-	-	2,447,181
Gross Investment Income	2,783,866,948	8,395,374	3,094,776	9,689	2,795,366,787
Less: Investment Expense	(22,160,690)	(61,078)	-	-	(22,221,768)
Less: Securities Lending Expense	(734,034)	-	-	-	(734,034)
Net Investment Income	2,760,972,224	8,334,296	3,094,776	9,689	2,772,410,985
Total Additions	4,101,171,036	281,216,147	4,763,598	69,689	4,387,220,470
Deductions					
Benefits	1,402,535,713	-	4,120,000	85,178	1,406,740,891
Refunds of Contributions	17,325,387	-	-	-	17,325,387
Insurance Expenses	-	226,435,363	-	-	226,435,363
Administrative Expense	7,322,739	1,186,029	21,511	445	8,530,724
Total Deductions	1,427,183,839	227,621,392	4,141,511	85,623	1,659,032,365
Net Increase(Decrease)	2,673,987,197	53,594,755	622,087	(15,934)	2,728,188,105
Net Assets Held In Trust For Pension And Other Postemployment Benefits					
Beginning of Year	12,456,619,082	241,223,840	87,904,593	986,036	12,786,733,551
End of Year	$ 15,130,606,279	$ 294,818,595	$ 88,526,680	$ 970,102	$ 15,514,921,656

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

NOTE 1: DESCRIPTION OF RETIREMENT ANNUITY PLAN

A. REPORTING ENTITY

The Teachers' Retirement System of the State of Kentucky (KTRS) was created by the 1938 General Assembly and is governed by Chapter 161 Section 220 through Chapter 161 Section 990 of the Kentucky Revised Statutes (KRS). KTRS is a blended component unit of the Commonwealth of Kentucky and therefore is included in the Commonwealth's financial statements. KTRS is a cost-sharing multiple-employer defined benefit plan established to provide retirement annuity plan coverage for local school districts and other public educational agencies in the state.

B. PARTICIPANTS

As of June 30, 2012 a total of 208 employers participated in the plan. Employers are comprised of 174 local school districts, 17 Department of Education Agencies and other educational organizations, 5 universities and also the Kentucky Community and Technical College System.

According to KRS 161.220 " . . . any regular or special teacher, or professional occupying a position requiring certification or graduation from a four (4) year college or university . . . " is eligible to participate in the System. The following illustrates the classifications of members:

	2012	2011
Active contributing members:		
Vested	48,383	47,945
Non-vested	27,568	28,404
Inactive members, vested	6,668	6,135
Retirees and beneficiaries currently receiving benefits	46,094	44,419
Total members, retirees, and beneficiaries	128,713	126,903

C. BENEFIT PROVISIONS

Members become vested when they complete five (5) years of credited service. To qualify for monthly retirement benefits, payable for life, members must either:

1.) Attain age fifty-five (55) and complete five (5) years of Kentucky service, or

2.) Complete 27 years of Kentucky service.

Participants that retire before age 60 with less than 27 years of service receive reduced retirement benefits. Non-university members receive monthly payments equal to two (2) percent (service prior to July 1, 1983) and two and one-half (2.5) percent (service after July 1, 1983) of their final average salaries for each year of credited service. University employees receive monthly benefits equal to two (2) percent of their final average salary for each year of credited service. The final average salary is the member's five (5) highest annual salaries except members at least 55 with 27 or more years of service may use their three (3) highest annual salaries. New members (including second retirement accounts started) after July 1, 2002 will receive monthly benefits equal to 2% of their final average salary for each year of service if, upon retirement, their total service is less than ten years. New members after July 1, 2002 who retire with ten or more years of total service will receive monthly benefits equal to 2.5% of their final average salary for each year of service, including the first ten years. In addition, non-university members who retire July 1, 2004 and later with more than 30 years of service will have their multiplier increased for all years over 30 from 2.5% to 3.0% to be used in their benefit calculation.

The System provides medical benefits to retirees as fully described in Note 8. The System also provides disability benefits for vested members at the rate of sixty (60) percent of the final average salary. A life insurance benefit, payable upon the death of a member, is $2,000 for active contributing members and $5,000 for retired or disabled members.

Cost of living increases are one and one-half (1.5) percent annually. Additional ad hoc increases and any other benefit amendments must be authorized by the General Assembly.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. BASIS OF ACCOUNTING

The financial statements are prepared on the accrual basis of accounting. Member contributions and employer matching are recognized in the fiscal year due. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

B. CASH

KTRS has five cash accounts. At June 30, 2012, the retirement annuity cash account totaled $24,131,311 and the administrative expense fund cash account was $1,183,201 for a total of $25,314,512 as carrying value of cash in the defined benefit plan. The medical insurance cash account totaled $5,202,577, the life insurance plan cash account totaled $299,153 and the excess benefit fund cash account contained $9,828. Therefore, the carrying value of cash was $30,826,070 and the bank balance was $38,615,798 and funds controlled by the Commonwealth of Kentucky of $4,555,141. The variance is primarily due to outstanding checks and items not processed by the bank on June 30, 2012.

C. CAPITAL ASSETS

Fixed assets are recorded at historical cost less straight-line accumulated depreciation. The classes of fixed assets are furniture and equipment, the KTRS office buildings and land. Furniture and equipment are depreciated over an average useful life of five years. The office buildings are depreciated over forty years. Internally created software for the Pathway capital project will be capitalized and amortized over fifteen years. The Pathway project will update technological record keeping abilities and improve timeliness and accuracy of responses to member inquiries.

D. INVESTMENTS

Plan investments are reported at fair value. Fair value is the amount that a plan can reasonably expect to receive for an investment in a current sale between a willing buyer and a willing seller. Short-term securities are carried at cost, which approximates fair value. Fixed income and common and preferred stocks are generally valued based on published market prices and quotations from national security exchanges and securities pricing services. Real estate is primarily valued based on appraisals performed by independent appraisers. Alternative investments such as private equity, timberland, and other additional categories are valued using the most recent general partner statement of fair value based on independent appraisals, updated for any subsequent partnership interests' cash flows.

Purchase and sales of debt securities, equity securities, and short-term investments are recorded on the trade date. Real estate equity transactions are recorded on the settlement date. Upon sale of investments, the difference between sales proceeds and cost is reflected in the statement of changes in plan net assets. Investment expenses consist of investment manager and consultant fees along with fees for custodial services.

E. COMPENSATED ABSENCES

Expenses for accumulated vacation days and compensatory time earned by the System's employees are recorded when earned. Upon termination or retirement, employees of the System are paid for accumulated vacation time limited to 60 days and accumulated compensatory time limited to 240 hours. As of June 30, 2012 and 2011 accrued compensated absences were $876,573 and $830,349.

F. RISK MANAGEMENT

Destruction of assets, theft, employee injuries and court challenges to administrative policy are among the various risks to which the System is exposed. In order to cover such risks the System carries appropriate insurance policies such as fire and tornado, employee bonds, fiduciary liability, worker's compensation and equipment insurance.

G. OTHER RECEIVABLES

KTRS allows qualified purchases of service credit to be made by installment payments not to exceed a five-year period. Revenue is recognized in the initial year of the installment contract agreement. The June 30, 2012 and 2011 installment contract receivables were $499,433 and $431,187.

The other receivables reported in the medical insurance fund consists primarily of Kentucky Retirement Systems' net cost of their retirees who elect to take their health benefits with KTRS in the amount of $3,873,520 for the 2012 fiscal year.

H. USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

I. INCOME TAXES

The defined benefit plan is organized as a tax-exempt retirement plan under the Internal Revenue Code. The tax sheltered annuity plan is no longer continued and will be fully terminated when all lifetime annuities have expired. The System's management believes that it has operated the plans within the constraints imposed by federal tax law.

J. RECENT PRONOUNCEMENTS

In June 2011, the GASB issued Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position. GASB Statement No. 63 provides financial reporting guidance relative to deferred outflows of resources, a consumption of net assets by KTRS that is applicable to a future reporting period, and deferred inflows of resources, an acquisition of net assets by KTRS that is applicable to a future reporting period. GASB Statement No. 63 incorporates deferred outflows and inflows of resources into the definitions of the required components of the residual measure, renaming such measure as net position, rather than net assets. The provisions of GASB Statement No. 63 are effective for fiscal periods beginning after December 15, 2011 (the fiscal year ended June 30, 2013). While KTRS has not yet evaluated the impact the provisions of GASB Statement No. 63 will have on its financial statements as of and for the year ended June 30, 2013, the adoption of this standard is not expected to have an impact on KTRS's financial position, results of operations, and/or cash flows.

NOTE 3: CONTRIBUTIONS AND RESERVES

A. CONTRIBUTIONS

Contribution rates are established by Kentucky Revised Statutes. Non-university members who joined the plan prior to July 2008 are required to contribute 10.355% of their salaries to the System; university members are required to contribute 8.715% of their salaries. KRS 161.565 allows each university to reduce the contribution of its members by 2.215%; therefore, university members contribute 6.50% of their salary to KTRS. Members who joined the plan on and after July 2008 are required to contribute an additional .50% to the medical insurance plan.

For members employed by local school districts, the state contributes 13.105% of salary for those who joined before July 1, 2008 and 14.105% for those after, except for those members who are employed in federally funded positions, in which case the federal program pays the required percentages. Other participating employers are required to contribute the percentage contributed by members plus an additional 3.25% of members' gross salaries.

The member and employer contributions consist of retirement annuity contributions and post-employment contributions to the medical insurance plan. The post-employment contribution from employee (1.25% for members prior to July 1, 2008 or 1.75% for members who joined after July 1, 2008) and the employer contribution rate of .75% of members' gross salaries funded KTRS's retiree medical insurance plan. Also, after July 1, 2010 employers (other than the state) contribute .50% of members' salaries and the state contributes the net cost of health insurance premiums for new retirees after June 30, 2010 in the non-Medicare eligible group. If a member leaves covered employment before accumulating five (5) years of credited service, accumulated member contributions to the retirement annuity plan plus interest are refunded upon the member's request.

The KTRS defined benefit retirement annuity plan received $465,384,165 in fiscal year 2011 in funding from the state in the form of bond proceeds which fully satisfied amortized payments that the state was making for amounts that were redirected to the medical insurance plan from fiscal year 2005 through fiscal year 2010.

B. RESERVES

Member Reserve

This fund was established by KRS 161.420(2) as the Teacher Savings Fund and consists of contributions paid by university and non-university members. The fund also includes interest authorized by the Board of Trustees from Unallocated Reserves. The accumulated contributions of members that are returned upon withdrawal or paid to the estate or designated beneficiary in the event of death are paid from this fund. Upon retirement, the member's contributions and the matching state contributions are transferred from this fund to Benefit Reserves, the fund from which retirement benefits are paid.

Employer Reserve

This fund was established by KRS 161.420(3) as the State Accumulation Fund and receives state appropriations to the Retirement System. The state matches an amount equal to members' contributions. State appropriations during the year are based on estimates of members' salaries. At year-end when actual salaries are known, the required state matching is also realized by producing either a receivable from or a payable to the State of Kentucky.

Benefit Reserve

This fund was established by KRS 161.420(4) as the Allowance Reserve Fund, the source for retirement, disability, and survivor benefits paid to members of the System. These benefits are paid from the retired members' contributions until they are exhausted, at which time state matching contributions are used to pay the benefits. After an individual member's contributions and the state matching contributions have been exhausted, retirement benefits are paid from monies transferred from Unallocated Reserves.

Unallocated Reserve

This fund was established by KRS 161.420(6) as the Guarantee Fund, to collect income from investments, state matching contributions of members withdrawn from the System, and state matching contributions for cost of living adjustments (COLAs). In addition, it receives money for which disposition is not otherwise provided. This fund provides interest to the other funds, benefits in excess of both members' and state matching contributions, monies for administrative expenses of the System, and deficiencies not covered by the other funds.

Administrative Expense Reserve

This fund was established by KRS 161.420(1) as the Expense Fund. Investment income transferred to this fund from Unallocated Reserves is used to pay the administrative expenses of the System. Starting July 1, 2010 administrative expenses are allocated among the funds based on benefits paid.

NOTE 4: FUNDED STATUS AND FUNDING PROGRESS

A. DESCRIPTION OF FUNDING PROGRESS

The funded status of the Defined Benefit Retirement Annuity Plan as of the most recent actuarial valuation date is as follows:

(Dollar amount in 1,000's)

Valuation Year June 30	Actuarial Value Of Assets A	Actuarial Accrued Liabilities B	Unfunded Actuarial Accrued Liabilities (UAAL) B-A	Funded Ratio (A/B)	Covered Payroll C	UAAL As a % of Covered Payroll [B-A/C]
2012	$ 14,691,371	$ 26,973,854	$ 12,282,483	54.5%	$ 3,479,567	353.0%

The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear funding trend information as obtained from the System's independent actuary's annual valuation report.

Expressing the actuarial value of assets as a percentage of the actuarial accrued liabilities provides an indication whether the System is becoming financially stronger or weaker. Generally, the greater the percentage the stronger the retirement system. Trends in unfunded actuarial accrued liabilities and annual covered payroll are both affected by inflation. Expressing the unfunded actuarial accrued liabilities as a percentage of annual covered payroll aids analysis of progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage the stronger the retirement system.

The accompanying schedule of employer contributions, presented as required supplementary information following the notes to the financial statements, presents trend information about the amounts contributed to the plan by employers in comparison to the Annual Required Contribution (ARC). The ARC is actuarially determined in accordance with the parameters of GASB Statement 50. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost for each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

B. METHODOLOGIES

The promised benefits of the System are included in the actuarially calculated contribution rates, which are developed using the entry age actuarial cost method. Gains and losses are reflected in the unfunded accrued liability that is being amortized by regular annual contributions as a level percentage of payroll within a 30-year period using an open amortization approach. The five (5) year smoothed market approach is used for asset valuation.

ACTUARIAL VALUE OF ASSETS

(1) Actuarial Value Of Assets On June 30,2011	$	14,908,138,356
(2) Market Value End Of Year June 30, 2012		14,797,120,889
(3) Market Value Beginning of Year June 30, 2011		15,130,606,279
(4) Cash Flow		
a. Contributions (exclusive of Pension Obligation Bond)		867,069,476
b. Benefit Payments		(1,502,488,237)
c. Administrative Expenses		(7,762,880)
d. Net		(643,181,641)
(5) Investment Income		
a. Market total: (2) - (3) -(4)d		309,696,251
b. Assumed Rate		7.5%
c. Amount for Immediate Recognition: [(3) x (5)b] + [(4)d * (5)b * 0.5]		1,110,676,159
d. Amount for Phased-In Recognition: (5)a - (5)c		(800,979,908)
(6) Phased-In Recognition of Investment Income		
a. Current Year: 0.20*(5)d		(160,195,982)
b. First Prior Year		363,670,625
c. Second Prior Year		133,378,916
d. Third Prior Year		(611,235,941)
e. Fourth Prior Year		(409,879,449)
f. Total Recognized Investment Gain		(684,261,831)
(7) Actuarial Value End of Year: (1) + (4)d + (5)c +(6)f		14,691,371,044
(8) Difference Between Market & Actuarial Values: (2) - (7)	$	105,749,845
(9) Rate of Return on Actuarial Value		2.92%

C. ASSUMPTIONS

Significant actuarial assumptions employed by the actuary for the funding purposes as of June 30, 2012, the most recent updated actuarial information include:

*	Assumed inflation rate	3.5%
*	Assumed investment rate	7.5%
*	Assumed projected salary increases	4.0% - 8.20%
*	Assumed annual cost of living adjustments	1.5%

NOTE 5: DEPOSITS WITH FINANCIAL INSTITUTIONS AND INVESTMENTS (Including Repurchase Agreements)

A. Legal Provisions for Investments

The following disclosures are meant to help the users of KTRS' financial statements assess the risks KTRS takes in investing member funds. The Board of Trustees and the Investment Committee are guided by asset allocation parameters that the Board approves through its powers as defined in KRS 161.430.

KTRS administers a retirement annuity trust fund, and a health insurance trust fund in accordance with state and federal law. KTRS provides service and disability retirement benefits, death and survivor benefits, health insurance benefits, and life insurance benefits for Kentucky public education employees and their beneficiaries. The trust funds managed by KTRS shall be referred to collectively as the "retirement system" unless the context requires a specific reference to a particular fund.

The asset allocation parameters for the retirement annuity trust fund are set forth in Title 102, Chapter 1:175, Section 2 of the Kentucky Administrative Regulations as follows:

- There shall be no limit on the amount of investments owned by the retirement annuity trust fund if the investments are guaranteed by the United States government.
- Not more than thirty-five percent (35%) of the assets of the retirement annuity trust fund at market value shall be invested in corporate debt obligations.
- Not more than ten percent (10%) of the assets of the retirement annuity trust fund at market value shall be invested in foreign debt.
- Not more than sixty-five percent (65%) of the assets of the retirement annuity trust fund at market value shall be invested in common stocks or preferred stocks. Not more than twenty-five percent (25%) of the assets of the retirement annuity trust fund at market value shall be invested in a stock portfolio designed to replicate a general stock index. Not more than thirty percent (30%) of the assets of the retirement annuity trust fund at market value shall be invested in the stocks of companies domiciled outside of the United States; any amounts so invested shall be included in the sixty-five percent (65%) limitation for total stocks.
- Not more than ten percent (10%) of the assets of the retirement annuity trust fund at market value shall be invested in real estate. This would include real estate equity, real estate lease agreements, and shares in real estate investment trusts.
- Not more than ten percent (10%) of the assets of the retirement annuity trust fund at market value shall be invested in alternative investments. This category may include private equity, venture capital, timberland, and infrastructure investments.
- Not more than fifteen percent (15%) of the assets of the retirement annuity trust fund at market value shall be invested in any additional category or categories of investments. The Board of Trustees shall approve by resolution such additional category or categories of investments.

The asset allocation parameters for the health insurance trust fund are set forth in Title 102, Chapter 1:178, Section 2 of the Kentucky Administrative Regulations as follows:

- In order to preserve the assets of the health insurance trust fund and produce the required rate of return while minimizing risk, assets shall be prudently diversified among various classes of investments.

- In determining asset allocation policy, the investment committee and the board shall be mindful of the health insurance trust fund's liquidity and its capability of meeting both short and long-term obligations.

B. Cash and Cash Equivalents

For cash deposits and cash equivalents, custodial credit risk is the risk that, in the event of a bank failure, the retirement system's deposits may not be returned to the system. The retirement system's total cash balance held at J.P. Morgan Chase Bank in noninterest bearing accounts on June 30, 2012 was $38,615,798. In addition to these funds, an amount of $4,555,141 represents funds transferred to and controlled by the Commonwealth of Kentucky.

On November 9, 2010, the FDIC issued a Final Rule implementing Section 343 of the Dodd-Frank Wall Street Reform and Consumer Protection Act that provides for unlimited insurance coverage of noninterest-bearing transaction accounts. Beginning December 31, 2010, through December 31, 2012, all noninterest-bearing transaction accounts are fully insured, regardless of the balance of the account, at all FDIC-insured institutions.

Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are:

a. uncollateralized,

b. collateralized with securities held by the pledging financial institution, or

c. collateralized with securities held by the pledging financial institution's trust department or agent but not in the depositor-government's name.

As of June 30, 2012, the retirement system's cash balance in the amount of $38,615,798 was not exposed to custodial credit risk since this amount was fully insured by the FDIC as outlined above.

C. Investments

All of the retirement system's assets are invested in short-term and long-term debt (bonds and mortgages) securities, equity (stock) securities, real estate, and alternative investments, including additional categories as permitted by regulation. These assets are reported at fair market value.

Investments are governed by the Board of Trustees' policies while the Board of Trustees and the Investment Committee shall execute their fiduciary responsibilities in accordance with the "prudent person rule", as identified in KRS 161.430 (2)(b). The prudent person rule establishes a standard for all fiduciaries, to act as a prudent person would be expected to act, with the "care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims".

The following chart represents the fair market values of the investments of the Kentucky Teachers' Retirement System for June 30, 2012.

Schedule of Market Value of Investments

	June 30, 2012	June 30, 2011
Cash Equivalents		
Repurchase Agreement	$ -	$ 58,200,000
Short-Term Cash Investments	671,112,791	674,203,417
Total Cash Equivalents	**671,112,791**	**732,403,417**
Fixed Income		
U. S. Government	503,083,086	614,166,764
Agency Bonds	244,307,582	354,226,324
Mortgage Backed Securities	199,146,287	243,091,496
Asset Backed Securities	60,608,480	52,940,222
Commercial Mortgage Backed Securities	295,710,595	346,576,905
Collateralized Mortgage Obligations	43,276,306	90,802,918
Municipal Bonds	511,058,651	509,893,503
Corporate Bonds	1,851,470,193	1,807,576,426
Total Fixed Income	**3,708,661,180**	**4,019,274,558**
Equities		
Global	140,740,862	150,698,032
International Equity	2,307,653,944	2,417,879,386
U.S. Preferred Equity	1,281,501	-
U. S. Equity	6,951,648,515	7,170,669,948
Total Equities	**9,401,324,822**	**9,739,247,366**
Real Estate		
Real Estate Equity	586,800,766	480,447,237
Total Real Estate Equity	**586,800,766**	**480,447,237**
Alternative and Additional Investments		
Additional Categories	313,203,119	207,077,927
Private Equity	266,581,754	189,131,442
Timberland	185,432,686	180,318,434
Total Alternative & Additional Investments	**765,217,559**	**576,527,803**
TOTAL INVESTMENTS	**$ 15,133,117,118**	**$ 15,547,900,381**

Custodial Credit Risk

Custodial Credit Risk for an investment is the risk that, in the event of the failure of counterparty, the pension trust fund will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the retirement system, and are held by either:

a. the counterparty, or

b. the counterparty's trust department or agent, but not in the System's name.

The cash reserve of the retirement system is primarily maintained in high quality short term investments through the Dreyfus Institutional Cash Advantage Fund. This Fund invests in a diversified portfolio of high quality, short-term debt securities and the Fund is rated AAA by S&P, Moody's, and Fitch, Inc. The Fund's portfolio is structured within the confines of Rule 2a-7 under the Investment Company Act of 1940, as amended. Commercial paper, U.S. Treasury and agency obligations, certificates of deposit, bankers' acceptances, repurchase agreements, time deposits, etc. are all permissible investments within this Fund.

Whenever repurchase agreements are ordered by KTRS under the terms of Master Repurchase Agreements with various brokers, the terms are dictated by KTRS. The repurchase agreements and their supporting collateral are held by the custodial agent's correspondent bank in an account identified by the custodian's name and KTRS' nominee name. This account is unique to KTRS. The Master Repurchase Agreements require that the supporting collateral have a market value of at least 102% of the value of the repurchase agreements.

As of June 30, 2012, cash collateral reinvestment securities acquired through securities lending for the retirement annuity trust fund by KTRS's custodian, who is also the lending agent/counterparty, amounted to $396,546,893 related to $391,348,088 securities lent consistent with the lending agreement with the custodian. (Please refer to a following section entitled Securities Lending.)

Interest Rate Risk

Interest rate risk on investments is the possibility that changes in interest rates will reduce the fair value of the retirement system's investments. In general, the longer the period until an investment matures, the greater the risk of a negative impact on fair value resulting from changes in interest rates.

As of June 30, 2012 KTRS had the following investments and weighted average maturities:

Investment Type	Fair Value	Average Maturity (Yrs)
U.S Government	$ 503,083,086	10.42
Agency	244,307,582	8.26
MBS	199,146,287	12.62
CMO	43,276,306	18.85
ABS	60,608,480	13.69
CMBS	295,710,595	28.07
Muni	511,058,651	14.58
Corporate	1,851,470,193	8.49
Total	$ 3,708,661,180	11.57

*This schedule includes **$272,005,420** of fixed income securities classified in additional categories.

In addition to the above securities, short-term cash investments in the Dreyfus Institutional Cash Advantage Fund and STIF held at the Bank of New York Mellon had a total fair value of $671,112,791 and had a weighted average maturity of thirty-seven (37) days. Average maturity is used as a measure of a security's exposure to interest rate risk due to fluctuations in market interest rates. Mortgage-backed securities and collateralized mortgage obligations are typically amortizing investments with an average life and interest rate risk significantly less than suggested by the legal maturity. Mortgage-backed securities, which are generally pre-payable, and other callable bonds are subject to adverse changes in average life in response to market interest rate changes. The schedule above reflects only the legal maturity of all such bonds.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. This risk is managed by using the effective duration or option adjusted methodology to quantify the risk of interest rate changes. This methodology takes into account optionality on bonds and scales the risk of price changes on bonds depending upon the degree of changes in rates and the slope of the yield curve. The control of interest rate risk is not set forth in a particular policy; however, the retirement system manages interest rate risk in practice by establishing appropriate benchmarks for its various portfolios.

Mortgage-backed securities are securities representing pass-through interests in the cash flows from pools of mortgage loans on single-family or multi-family residential properties. All of the mortgage-backed securities owned by the retirement system were securitized and are guaranteed by Fannie Mae, Freddie Mac, or GNMA. The average life of a mortgage-backed security depends upon the level of prepayments experienced in the underlying pool of loans. Market interest rates are a primary determinant of prepayment levels. Lower than anticipated market rates generally lead to higher than anticipated prepayments and a shorter average life; higher than anticipated market rates generally lead to lower than anticipated prepayments and a longer average life. The retirement system held $199.1 million in mortgage-backed securities as of June 30, 2012.

Collateralized mortgage obligations are bonds that are collateralized by whole loan mortgages, mortgage pass-through securities or stripped mortgage-backed securities. Income is derived from payments and prepayments of principal and interest generated from collateral mortgages. Cash flows are distributed to different investment classes in accordance with a collateralized mortgage obligations established payment order. The System held $43.3 million in collateralized mortgage obligations as of June 30, 2012.

Asset-backed securities are bonds or notes backed by loan paper or accounts receivable originated by banks, credit card companies, or other credit providers. The originator of the loan or accounts receivable paper sells it to a specially created trust, which repackages it as securities. Asset-backed securities have been structured as pass-throughs and as structures with multiple bond classes. The asset-backed securities in the amount of $60.6 million, held by the retirement system as of June 30, 2012, are moderately sensitive to changes in interest rates.

Commercial mortgage-backed securities are securities representing interests in the cash flows from pools of mortgage loans on commercial properties. The interests in a securitized pool of loans are generally divided into various tranches based upon planned payment order and level of seniority. The retirement system's commercial mortgage-backed securities investments consist of highly rated relatively senior tranches. The average maturity of the retirement system's commercial mortgage-backed securities holdings in the schedule above reflects the legal maturity of those holdings. Most of the tranches held are earlier in the planned payment order than the legal maturity suggests. The retirement system held $295.7 million in commercial mortgage-backed securities investments as of June 30, 2012.

Credit Risk

Credit risk is the risk that an issuer or counterparty to an investment will not fulfill its obligations. The following schedule lists retirement system's fixed income investments (net of cash equivalents) according to credit ratings as of June 30, 2012:

Rating		Fair Value	%
U.S. Government	$	503,083,087	13.6%
AAA		492,680,759	13.3%
AA		995,406,618	26.8%
A		758,182,293	20.4%
BBB		636,145,588	17.2%
BB		137,417,611	3.7%
B		181,166,681	4.9%
CCC		4,578,544	0.1%
Total	**$**	**3,708,661,180**	**100.0%**

*This schedule includes **$272,005,420** of fixed income securities classified in additional categories.

Total market value of the fixed income portfolio was $3,708,661,180 on June 30, 2012. The rating system used in the chart is the nationally recognized Standard & Poor's rating system.

In addition to the above categories, the retirement system held $671,112,791 in short term investments through the Dreyfus Institutional Cash Advantage Fund. The credit risk associated with this Fund is minimal as the securities held are required to maintain the highest possible short-term credit ratings by Moody's and Standard & Poor's. In addition, investments in US Government and Agency securities are also highly rated securities since they are backed by the US Government. Notation is made that the ratings of securities is subject to change due to circumstances and thereby may have a lower rating than when first purchased.

The retirement annuity trust fund's policy on credit rating is set forth in 102 KAR 1:175 and reads as follows:

"A fixed income investment shall be rated at the time of purchase as investment grade by at least one (1) of the major rating services. A private placement debt investment shall be subject to the same credit qualifications as each fixed income investment. The fixed income investment portfolio as a whole shall maintain an average rating of investment grade by at least one (1) of the major rating services."

Concentration of credit risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Losses from credit risk are heightened if a significant portion of resources are invested with a single issuer. Per Administrative Regulation 102 KAR 1:175, the retirement annuity trust fund is subject to the following policies regarding single issuers of fixed income and equity securities:

"Unless the issuer is the United States Government or a government sponsored enterprise (GSE), the amount invested in the securities of a single issuer shall not equal more than five percent (5%) of the assets of the system.

"The System's position in a single stock shall not exceed two and one-half percent (2.5%) of the System's assets. The system's position in a single stock shall not exceed five percent (5%) of the outstanding stock for that company unless the investment is part of a venture capital program."

KTRS has not invested greater than five percent (5%) of the retirement annuity trust fund's assets at market value in any single issuer and is in compliance with investment policy.

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. As of June 30, 2012, the retirement system’s exposure to foreign currency risk consisted of $2,564,615,958 of foreign investments.

The following amounts represent the market values of investments that are subject to foreign currency as a result of cash contributions to each portfolio manager.

Investment		Amount
Commingled Funds		
UBS International Collective	$	655,036,895
Baillie Gifford		535,638,515
Baring Asset Management		388,140,136
Black Rock Fund B		73,055,358
Alternative Funds		
KKR & Co European Fund III		37,466,724
Oaktree European Principal Fund III		7,561,954
Fixed Income Securities (Misc Funds)		177,129,968
Equity Securities (ADR's)		690,586,408
Total	$	2,564,615,958

The following table reflects the various foreign currencies associated with the retirement system's investments in the funds outlined above:

Currency	Market Value
Austrailian Dollar	$ 135,452,957
Bermudian Dollar	12,972,885
Brazilian Real	66,644,745
British Pound Sterling	437,457,420
Canadian Dollar	198,176,265
Cayman Islands Dollar	8,343,708
Chilean Peso	3,400,242
Chinese Yuan	142,014,107
Colombian Peso	8,677,301
Czech Crown	55,214
Danish Krone	33,887,931
Egyptian Pound	65,781
Euro	457,450,912
Hong Kong Dollar	70,763,526
Hungarian Forint	48,236
Indian Rupee	7,018,758
Indonesian Rupiah	12,014,734
Israeli New Shekel	46,178,752
Japanese Yen	290,285,010
Jersey Pound	5,266,700
Malaysian Ringgit	6,238,102
Malian Franc	4,795,897
Mexican Peso	50,854,224
Moroccan Dirham	16,674
New Zealand Dollar	94,344
Norwegian Krone	20,365,283
Panamanian Balboa	7,423,200
Papua New Guinea Kina	3,176,493
Peruvian Nuevo Sol	4,159,516
Philippine Peso	179,443
Polish Złoty	8,964,135
Russian Ruble	61,018,872
Singapore Dollar	43,547,494
South African Rand	14,260,974
South Korean Won	76,672,264
Swedish Krona	92,456,804
Swiss Franc	179,152,580
Taiwan Dollar	34,120,691
Thai Baht	9,997,268
Turkish Lira	7,672,924
Various	3,273,593
Grand Total	**$ 2,564,615,958**

The majority of foreign investments are held in commingled funds managed by UBS Global Asset Management, Baillie Gifford, Baring Asset Management, and Black Rock. In addition to the commingled funds investing in foreign securities, the retirement annuity trust fund held $690,586,408 associated with foreign interests in American Depositary Receipt investments. These American Depositary Receipts are securities that are issued by a U.S. bank in place of the foreign stock shares held in trust by that bank, thereby facilitating the trading of foreign shares in U.S. markets. American Depositary Receipts are denominated in U.S. currency. Other foreign securities and investments consisted of debt securities and alternative investment opportunities.

The retirement annuity trust fund's policy regarding foreign equities is that not more than thirty percent (30%) of the assets of the retirement annuity trust fund at market value shall be invested in the stocks of companies domiciled outside of the United States. Any amounts so invested shall be included in the sixty-five percent (65%) limitation for total stocks per 102 KAR 1:175 Section 2(e).

D. Securities Lending

Section 161.430 of the Kentucky Revised Statutes empowers the Board of Trustees with complete fiduciary responsibility for the funds of the retirement system. The retirement system operates a securities lending program in which it temporarily lends securities to qualified agents in exchange for a net fee and high quality collateral. U.S. Government and agency securities, selected domestic bonds, and domestic and international stocks are the types of securities that are lent. The retirement system's custodian, The Bank of New York Mellon, acts as lending agent in exchanging securities for collateral. The collateral has a value of not less than 102% of the market value of the lent securities plus any accrued, unpaid distributions. The collateral may consist of cash, marketable U.S. Government securities, and select marketable U.S. Government agency securities approved by the retirement system.

Securities lending transactions are accounted for in accordance with GASB Statement No. 28 Accounting and Financial Reporting for Securities Lending Transactions, which established standards of accounting and financial reporting for securities lending transactions. During the fiscal year ended June 30, 2012, only the retirement annuity trust fund had securities lending transactions. The following section details the net income earned in the retirement annuity trust fund from securities lending for the fiscal year ended June 30, 2012:

Item		Earnings
Gross Earnings (Interest and Fees)	$	314,708
Gross Borrower Rebates	$	2,790,509
Less: Bank Fees	$	(931,520)
Net Earnings	**$**	**2,173,697**

Cash collateral is invested in short-term obligations fully guaranteed by the United States Government or select Government agencies and Government Repurchase Agreements with qualified agents. The retirement system cannot pledge or sell collateral securities received unless the borrower defaults. The lending agent (Bank of New York Mellon) also indemnifies the retirement system from any financial loss associated with a borrower's default and collateral inadequacy.

As of June 30, 2012 the loan average days to maturity in the retirement annuity trust fund was three (3) days and the weighted average investment maturity of cash collateral investments was three (3) days. At fiscal year end, the retirement annuity trust fund had no credit risk exposure to borrowers, since the amounts the retirement annuity trust fund owes the borrowers exceeds the amounts the borrowers owe the retirement annuity trust fund and there were no losses resulting during the period.

Security lending programs can entail interest rate risk and credit risk. The retirement system minimizes interest rate risk by limiting the term of cash collateral investments to several days. The credit risk is controlled by investing cash collateral in securities with qualities similar to the credit worthiness of lent securities.

The following table presents the fair values of the underlying securities, and the value of the collateral pledged at June 30, 2012:

Type of Security Lent	Fair Value	Cash & Non-cash Collateral Value* Received
Fixed Income	$ 184,747,586	$ 191,392,812
Equities	206,600,502	205,154,081
Total	**$ 391,348,088**	**$ 396,546,893**

*Represents value of cash collateral only. Loan or margin collateral requirements met via the use of non-cash collateral (e.g. Government securities or Letters of Credit) are excluded from these values.

NOTE 6: RETIREMENT PLAN FOR EMPLOYEES OF THE SYSTEM

Full-time employees of Kentucky Teachers' Retirement System (KTRS) participate in either KTRS or Kentucky Employees Retirement System. Both plans are multiple-employer cost sharing defined benefit retirement annuity plans. All KTRS employees in positions requiring a four-year degree are covered under KTRS. The contribution rates and required employer matching are the same as state agency employers in the System. These rates, the plan description and funding policy are fully disclosed in the notes to the financial statements.

The System's annual required contributions for KTRS employee members for the fiscal years 2012, 2011 and 2010 were \$533,378, \$469,896, and \$476,918 respectively. KTRS contributed 100% of the required contribution each year.

All other KTRS employees are covered under the Kentucky Employee Retirement System (KERS) in the Non-Hazardous Employees Pension Plan. The plan provides for retirement, disability, and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under certain circumstances. Per KRS 61.565(3), contribution rates shall be determined by the Board on the basis of an annual actuarial valuation. Rates may be amended by the Board as needed. The System's administrative budget and employer contribution rates are subject to the approval of the Kentucky General Assembly. Employee contribution rates are set by the statute and may be changed only by the Kentucky General Assembly.

Members of KERS who joined prior to July 1, 2008, are required to contribute 5% of their annual creditable compensation for the fiscal years 2012, 2011 and 2010 and members who joined on or after July 1, 2008 contribute an additional 1%. As the employer, KTRS is required to contribute the annual actuarially determined rate of the creditable compensation (or the rate approved by legislators). The approved rate for the fiscal years 2012, 2011 and 2010 were 23.61%, 16.98%, and 11.61% and the System's annual required contributions to KERS were \$350,869, \$241,899, and \$174,203 respectively. KTRS contributed 100% of the required contributions for each year.

KERS issues a publicly available financial report that may be obtained by writing Kentucky Retirement System, 1260 Louisville Road, Frankfort, Kentucky 40601-6124.

NOTE 7: OTHER FUNDS

A. 403(B) TAX-SHELTERED ANNUITY PLAN

Plan Description

KTRS has, in prior years, administered a salary deferral program as permitted by section 403(b) of the Internal Revenue Code. Under this program members were able to voluntarily defer a portion of their compensation within the limits established by the applicable laws and regulations. However, the System's Board of Trustees determined that the cost of providing the necessary services to assure the System of continuing compliance with these laws and regulations was not economically feasible due to the limited participation in the program by the System's members. The Board decided, therefore, to discontinue offering the program as of April 30, 1997. Members who were not receiving annuities from their account as of April 30, 1997, were able to transfer their respective accounts directly into other tax-sheltered plans on a tax-free basis. As of June 30, 2012, the fourteen members who are receiving annuities will continue to receive distributions according to the terms of their respective elections.

Summary of Significant Policies

Basis of Accounting - The Tax-sheltered Annuity Plan financial statements are prepared using an accrual basis of accounting. Contributions are no longer being accepted into the plan; therefore, there are no receivables to be recognized.

Method Used to Value Investments - The short-term investments are reported at cost, which approximates fair value.

B. SUPPLEMENTAL BENEFIT FUND

The Supplemental Retirement Benefit Fund is a qualified governmental excess benefit arrangement as described in Section 415 of the Internal Revenue Code. In accordance with KRS 161.611 and KRS 161.420(8), KTRS is authorized to provide a supplemental retirement benefit fund for the sole purpose of enabling the employer to apply the same formula for determining benefits payable to all members of the retirement system employed by the employer, whose benefits under the retirement system are limited by Section 415 of the Internal Revenue Code of 1986, as amended from time to time. Funding of benefits payable under this fund are provided by the state, as employer, and are segregated from funds that are maintained by KTRS for payment of the regular benefits provided by the retirement system.

C. JUNITA LOSEY SCHOLARSHIP BEQUEST

Junita Losey, a retired teacher, designated KTRS as a residuary beneficiary of her estate and expressed a desire that KTRS establish a scholarship program for Kentucky students studying to be teachers. Ms. Losey died in 1997 and thereafter her estate provided a scholarship bequest to KTRS. The scholarship bequest has at all times been segregated from funds that are maintained by KTRS for payment of the regular benefits provided by the retirement system. The Scholarship Committee of the System's Board of Trustees meets each December to consider scholarship standards and administration of the scholarship bequest.

NOTE 8: MEDICAL INSURANCE PLAN AND POST-EMPLOYMENT BENEFITS

A. PLAN DESCRIPTION

In addition to the retirement annuity plan described in Note 1, Kentucky Revised Statute 161.675 requires KTRS to provide access to post-employment healthcare benefits for eligible members and dependents. The KTRS medical plan is funded by employer and member contributions. Changes made to the medical plan may be made by the KTRS Board of Trustees, the Kentucky Department of Employee Insurance and the General Assembly.

The KTRS medical plan is funded by employee contributions to an account established pursuant to 26 U.S.C. sec. 401(h). Additional funding is derived from the Kentucky Teachers' Retirement System insurance trust fund that went into effect on July 1, 2010. The insurance trust fund provides a trust separate from the account established pursuant to 26 U.S.C. sec. 401(h). The insurance trust fund includes employer and retired member contributions required under KRS 161.550 and KRS 161.675(4)(b).

To be eligible for medical benefits, the member must have retired either for service or disability. The KTRS medical plan offers coverage to members under the age of 65 through the Kentucky Employees Health Plan administered by the Kentucky Department of Employee Insurance. KTRS retired members are given a supplement to be used for payment of their health insurance premium. The amount of the member's supplement is based on a contribution supplement table approved by the KTRS Board of Trustees. The retired member pays premiums in excess of the monthly supplement. The Commonwealth of Kentucky bears risk for excess claims expenses that exceed the premium equivalents charged for the Kentucky Employees Health Plan. Once retired members and eligible spouses attain age 65 and are Medicare eligible, coverage is obtained through the KTRS Medicare Eligible Health Plan.

At June 30, 2012, KTRS insurance covered 36,000 retirees and 7,008 dependents. There are 208 participating employers and 75,951 active members contributing to the medical plan.

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The KTRS medical plan financial statements are prepared using the accrual basis of accounting. Member contributions and employer matching are recognized in the fiscal year due.
Healthcare premiums charged to retired members are recognized when due and any premiums collected in advance are recognized as a liability.

Method Used to Value Investments

Since the investments are all short-term investments they are reported at cost, which approximates fair value.

C. CONTRIBUTIONS

The post-employment healthcare benefit provided by KTRS is financed on a pre-funded basis beginning July 1, 2010 with the implementation of the Shared Responsibility Plan. In order to fund healthcare benefits, active member contributions are matched by the state at .75% of members' gross salaries. Those members who joined the System before July 1, 2008 contributed 0.75% of gross payroll to the KTRS medical plan and beginning July 1, 2010 the contribution increases incrementally to 3.75% by July 1, 2015 under the Shared Responsibility Plan. Member contributions to the KTRS medical plan are 1.75% of gross payroll for those who joined the System after July 1, 2008 and beginning July 1, 2010 the contribution increases incrementally to 3.75% by July 1, 2015 under the Shared Responsibility Plan. Also, the premiums collected from retirees and investment income contributes to funding the plan. The KTRS medical plan received $268,400,000 in fiscal year 2011 in funding from the state, which was contributed to the insurance trust fund. This transitional funding and increased contributions are for the 2011 and 2012 fiscal years.

D. FUNDED STATUS AND FUNDING PROGRESS

The funded status of the KTRS medical plan as of the most recent actuarial valuation date is as follows:

(Dollar amount in 1,000's)

Valuation Year June 30	Actuarial Value Of Assets A	Actuarial Accrued Liabilities B	Unfunded Actuarial Accrued Liabilities (UAAL) B-A	Funded Ratio (A/B)	Covered Payroll C	UAAL As a % of Covered Payroll [B-A/C]
2012	$ 338,746	$ 3,594,540	$ 3,255,794	9.4%	$ 3,479,567	93.6%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedules of funding progress, presented as required supplementary information following the notes to the financial statements, present multiyear trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

The accompanying schedule of employer contributions present trend information about the amounts contributed to the plan by employers in comparison to the ARC, an amount that is actuarially determined in accordance with the parameters of GASB Statement 43. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost for each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

Significant actuarial methodologies and assumptions employed as of the June 30, 2012 valuation date include the following:

Actuarial cost method	Entry Age
Actuarial value of assets	Market value of assets
Assumed inflation rate	3.5%
Investment rate of return	8.0%
Amortization method	Level percent of pay, open
Remaining amortization period	30 years
Medical Trend Assumption (Pre-Medicare)	9.50% - 5.0%
Medical Trend Assumption (Post-Medicare)	7.50% - 5.0%
Year of Ultimate Pre-Medicare trend rate	2019

E. INCURRED BUT NOT REPORTED CLAIMS LIABILITIES

KTRS recognizes estimates of liabilities for self-insured unpaid claims that have incurred (both reported and unreported) using the development method. This method uses past observed patterns of time between the date the claim is incurred and the date the claim is paid to estimate incurred claims from available paid claim information.

The following schedule shows the change in the claims and liability and the claims activity for the years ended June 30, 2012 and 2011.

	Fiscal Year 2012	Fiscal Year 2011
Unpaid Claims Liability	$ 403,000	$ 3,827,483
Current Year Claims and Changes in Estimates	189,926,846	177,509,547
Claims Payments	(190,262,846)	(180,934,030)
Ending Unpaid Claims Liability	$ 67,000	$ 403,000

NOTE 9: LIFE INSURANCE PLAN

A. PLAN DESCRIPTION

KTRS administers the Life Insurance Plan as provided by KRS 161.655 to provide life insurance benefits to retired and active members. This benefit is financed by actuarially determined contributions from the 208 participating employers. The benefit is $5,000 for members who are retired for service or disability, and $2,000 for active contributing members.

B. SUMMARY OF SIGNIFICANT POLICIES

Basis of Accounting

The Life Insurance Plan financial statements are prepared using the accrual basis of accounting. Employer contributions are recognized in the fiscal year due.

Method Used to Value Investments

Life Insurance Plan investments are reported at fair value. The short-term securities are carried at cost, which approximates fair value. Fixed income is generally valued based on published market prices and quotations from national security exchanges and securities pricing services.

C. CONTRIBUTIONS

To finance the life insurance benefit a portion of the employer contribution rate is directed to the plan as recommended by the KTRS's actuary. For both fiscal years 2012 and 2011, this rate has been .05% of active members' payroll.

D. FUNDED STATUS AND FUNDING PROGRESS

The funded status of the Life Insurance Plan as of the most recent actuarial valuation date is as follows:

(Dollar amount in 1,000's)

Valuation Year June 30	Actuarial Value Of Assets A	Actuarial Accrued Liabilities B	Actuarial Accrued Liabilities (UAAL) B-A	Funded Ratio (A/B)	Covered Payroll C	UAAL As a % of Covered Payroll [B-A/C]
2012	$ 92,241	$ 91,398	$ (843)	100.9%	$ 3,479,567	(0.02)

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. The required supplementary schedules following the notes to the financial section contain more actuarial information. Significant actuarial methodologies and assumptions employed as of the June 30, 2012 valuation date include the following:

Actuarial cost method	Entry Age
Actuarial value of assets	Market value of assets
Assumed inflation rate	3.5%
Investment rate of return	7.5%
Projected salary increases	4.0%
Amortization method	Level percent of pay, open
Remaining amortization period	30 years

Defined Benefit Plan
Schedule of Funding Progress
(dollar amounts in millions)

Valuation Year June 30	Actuarial Value of Assets A	Actuarial Accrued Liabilities B	Unfunded Actuarial Accrued Liabilities (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll C	UAAL As a % Of Covered Payroll [(B-A)/C]
2007	$ 15,285.0	$ 21,255.0	$ 5,970.0	71.9%	$ 2,975.3	200.7%
2008	15,321.3	22,460.3	7,139.0	68.2	3,190.3	223.8
2009	14,885.9	23,400.3	8,514.4	63.6	3,253.1	261.7
2010	14,851.3	24,344.3	9,493.0	61.0	3,321.6	285.8
2011	14,908.1	25,968.7	11,060.6	57.4	3,451.8	320.4
2012	14,691.4	26,973.9	12,282.5	54.5	3,479.6	353.0

The amounts reported in this schedule of funding progress do not include assets or liabilities for postemployment benefits, nor are the assets and liabilities of the tax-sheltered annuity plan included.

Defined Benefit Plan Schedule of Employer Contributions

Fiscal Year June 30	Annual Required Contributions	Actual Employer Contributions		Percentage Contributed
2007	$ 494,565,369	$ 434,890,469		88
2008	563,789,483	466,247,783		83
2009	600,282,735	442,549,935		74
2010	633,938,088	479,805,088		76
2011	678,741,428	1,037,935,993	*	153
2012	757,822,190	557,339,552		74

* Includes Pension Obligation Bond proceeds of $465,384,165

Medical Insurance Plan-Schedule of Funding Progress
(dollar amounts in millions)

Valuation Year June 30	Actuarial Value of Assets A	Actuarial Accrued Liabilities B	Unfunded Actuarial Accrued Liabilities (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll C	UAAL As a % Of Covered Payroll [(B-A)/C]
2007	$ 140.8	$ 5,928.8	$ 5,788.0	2.4%	$ 2,975.3	194.5
2008	185.9	6,434.5	6,248.6	2.9	3,190.3	195.9
2009	229.1	6,454.7	6,225.6	3.5	3,253.1	191.4
2010	241.2	3,206.8	2,965.6	7.5	3,321.6	89.3
2011	294.8	3,423.1	3,128.3	8.6	3,451.8	90.6
2012	338.7	3,594.5	3,255.8	9.4	3,479.6	93.6

The amounts reported in this schedule of funding progress do not include assets or liabilities for the defined benefit or life insurance plans, nor are the assets and liabilities of the tax-sheltered annuity plan included.

Medical Insurance Plan
Schedule of Employer Contributions

Valuation Year June 30	Annual Required Contributions(ARC) (A)	Actual Employer Contribution (B)	Retiree Drug Subsidy Contribution (C)	Total Contribution (B) + (C)	Percentage Of ARC Contributed [(B) + (C)/(A)]
2007	$ 231,473,321	$ 113,258,761	$ 10,312,361	$ 123,571,122	53.4%
2008	395,282,164	148,954,644	11,911,565	160,866,209	40.7%
2009	467,312,904	164,480,119	13,611,748	178,091,867	38.1%
2010	457,054,117	158,765,496	14,614,285	173,379,781	37.9%
2011	477,723,070	188,453,929	280,585	188,734,514	39.5%
2012	470,217,067	177,450,206	297,639	177,747,845	37.8%

Life Insurance Plan
Schedule of Funding Progress
(dollar amounts in thousands)

Valuation Year June 30	Actuarial Value of Assets A	Actuarial Accrued Liabilities B	Accrued Liabilities (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll C	As a % Of Covered Payroll [(B-A)/C]
2007	$ 71,426	$ 82,722	$ 11,296	86.3%	$ 2,975,289	0.38%
2008	77,658	84,265	6,607	92.2%	3,190,332	0.21
2009	84,703	90,334	5,631	93.8%	3,253,077	0.17
2010	87,905	92,091	4,186	95.5%	3,321,614	0.13
2011	88,527	88,088	(439)	100.5%	3,451,756	(0.01)
2012	92,241	91,398	(843)	100.9%	3,479,567	(0.02)

The amounts reported in this schedule of funding progress do not include assets or liabilities for the defined benefit or medical insurance plans, nor are the assets and liabilities of the tax-sheltered annuity plan included.

Life Insurance Plan
Schedule of Employer Contributions

Year Ended	Required Contributions(ARC)	Employer Contribution	Percentage Of ARC Contributed
2007	$ 1,785,173	$ 5,022,137	281.3%
2008	1,914,199	5,411,249	282.7%
2009	1,498,076	5,455,473	364.2%
2010	1,992,969	1,966,826	98.7%
2011	1,725,878	1,668,822	96.7%
2012	1,732,831	1,684,711	97.2%

Supporting Schedule 1
Schedule of Administrative Expenses

Salaries	$	6,396,770
Other Personnel Costs		692,250
Professional Services and Contracts		327,192
Utilities		90,501
Rentals		20,005
Maintenance		123,873
Postage & Related Services		342,433
Printing		110,040
Insurance		135,510
Miscellaneous Services		108,308
Telecommunications		36,565
Computer Services		140,669
Supplies		62,053
Depreciation		101,396
Travel		36,172
Dues & Subscriptions		44,945
Miscellaneous Commodities		14,357
Furniture, Fixtures, & Equipment not Capitalized		158,612
Compensated Absences		46,224
Total Administrative Expenses	$	8,987,875

Supporting Schedule 2
Schedule of Contracted Investment Management Expenses

	Pension	Medical	Total
Equity Managers			
Baillie Gifford	$ 2,058,808	$ -	
Baring Asset Management, Inc.	1,952,455	-	
Black Rock	-	89,693	
GE Asset Management	800,000	-	
Todd-Veredus Asset Management LLC	1,204,513	-	
UBS Global Asset Management	2,736,797	-	
Wellington Management Company	2,563,239	-	
Total Equity Managers	11,315,812	89,693	$ 11,405,505
Fixed Income Managers			
Fort Washington Investment Advisors	716,490	106,932	
Galliard Capital Management	322,081	-	
Total Fixed Income Managers	1,038,571	106,932	1,145,503
Real Estate	2,222,883	-	2,222,883
Alternative Investments	11,977,439	75,000	12,052,439
Custodian			
The Bank of New York Mellon	304,842	4,998	309,840
Consultant			
Hewitt Enis Knupp, Inc.	358,720	-	358,720
Legal & Research			
Schottenstein, Zox & Dunn	8,707	-	
Ice Miller	33,210	5,785	
Bevis Longstreth	50,417	-	
George Philip	30,000	-	
Miscellaneous	1,982	-	
Total Legal & Research	124,316	5,785	130,101
Other			
Subscription/Services	745,977	-	745,977
Total Contracted Investment Management Expenses	$ 28,088,560	$ 282,408	$ 28,370,968

Supporting Schedule 3
Schedule of Professional Services and Contracts

Professional	Nature of Service	Amount
Cavanaugh Macdonald Consulting	Actuarial Services	$ 140,250
Charles T. Mitchell Company	Auditing Services	30,825
Farmers Bank	Bank Services	15,149
International Claim Specialist	Investigative Services	1,600
Groom Law Group	Attorney Services	30,000
Ice Miller	Attorney Services	86,265
Reinhart, Boerner VanDeuren	Attorney Services	661
Stoll Keenon Ogden	Attorney Services	771
Wyatt Tarrant and Combs	Attorney Services	10,869
Digital Business Solutions	Website Design Consultant	10,802
Total Professional Services and Contracts		$ 327,192

Supporting Schedule 4
Combining Statement of Plan Net Assets
Other Funds

	403(b) Tax Shelter	Supplemental Benefit Fund	Losey Scholarship	Total
Assets				
Cash	$ -	$ 9,828	$ -	$ 9,828
Receivables				
Investment Income	-	-	1,183	1,183
Investments at Fair Value				
Short Term Investments	405,136	-	267,879	673,015
Bonds and Mortgages	-	-	270,532	270,532
Total Investments	405,136	-	538,411	943,547
Total Assets	405,136	9,828	539,594	954,558
Liabilities				
Due to Other Trust Funds	229	513	183	925
Net Assets Held In Trust For Pension And Other Benefits	$ 404,907	$ 9,315	$ 539,411	$ 953,633

Supporting Schedule 5
Combining Statement of Changes in Plan Net Assets
Other Funds

	403(b) Tax Shelter	Supplemental Benefit Fund	Losey Scholarship	Total
Additions				
Contributions				
Employer	$ -	$ -	$ -	$ -
Investment Income				
Net Appreciation/(Depreciation) in				
Fair Value of Investments	-	-	66,220	66,220
Interest	713	-	9,310	10,023
Net Investment Income	713	-	75,530	76,243
Total Additions	713	-	75,530	76,243
Deductions				
Benefits	18,952	55,280	18,000	92,232
Administrative Expense	99	288	93	480
Net Increase (Decrease)	(18,338)	(55,568)	57,437	(16,469)
Net Assets Held In Trust For				
Pension And Other Benefits				
Beginning of Year	423,245	64,882	481,975	970,102
End of Year	$ 404,907	$ 9,314	$ 539,412	$ 953,633

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Trustees
Teachers' Retirement System of the State of Kentucky
Frankfort, KY

We have audited the statement of plan net assets of the Teachers' Retirement System of the State of Kentucky, as of and for the year ended June 30, 2012, and the related statement of changes in plan net assets for the year then ended and have issued our report thereon dated December 17, 2012. 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.

Internal Control Over Financial Reporting

Management of the Teachers' Retirement System of the State of Kentucky is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Teachers' Retirement System of the State of Kentucky's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Teachers' Retirement System of the State of Kentucky's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Teachers' Retirement System of the State of Kentucky's internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Teachers' Retirement System of the State of Kentucky's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. 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*.

This report is intended solely for the information and use of management, the Board of Trustees, the Commonwealth of Kentucky, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.

Mountjoy Chilton Medley LLP

Lexington, KY
December 17, 2012