TEACHERS' RETIREMENT SYSTEM
of the State of Kentucky

GARY L. HARBIN, CPA
*Executive Secretary*

ROBERT B. BARNES, JD
*Deputy Executive Secretary*
*Operations and General Counsel*

ERIC WAMPLER, JD
*Deputy Executive Secretary*
*Finance and Administration*

**TO:** PPOB Staff
**FROM:** Beau Barnes, Deputy Executive Secretary and General Counsel
**DATE:** May 17, 2024
**SUBJECT:** Follow-up questions

This is TRS's response to the May 2, 2024, memorandum regarding questions from the Public Pension Oversight Board meeting of April 22.

Reporting of Sick Leave Information as Specified in 24 RS SB 4 HCS 1

No legal provision directly requires the information listed under SB 4 HCS 1 to be reported to TRS. The direct requirement under KRS 161.643(1) is that school districts are required to provide "an annual summary report of days employed and compensation paid" for TRS-covered employees.

Indirectly, the same subsection contains a requirement to report "other data as required by administrative regulation of the board of trustees." An administrative regulation cannot assume authority that is not provided explicitly. The "other data" language might be broad enough to include the sick leave data described in SB 4 HCS 1, however this would be an interpretation. The primary purpose of this statute is for TRS to collect the compensation and service credit data needed to calculate the retirement allowances of its members upon their retirement.

As background, the actuary does factor in and assumes an amount of sick leave when projecting overall liabilities − although the specific amount assigned to sick leave liability is not broken out from that overall liability. The history of sick leave shows that the days accrued and paid at retirement has been steady with most retirees never having any sick leave payouts. The data shows little fluctuation.

Some of the questions at the last PPOB meeting regarding sick leave accruals, including accruals through conversions of other leave to sick leave, are education policy matters beyond the TRS's statutory role. Accordingly, since TRS cannot respond TRS asked KDE to answer the question.

KDE's response:

> KRS 161.155(2) provides that "[e]ach district board of education shall allow each teacher and full-time employee in its common school system **not less than** ten (10) days of sick leave during each school year." That is, school districts can provide employees with more than 10 sick days annually, but not less than 10 sick days. Furthermore, the statute provides

that "[d]ays of sick leave not taken by an employee or teacher during any school year shall accumulate without limitation and be credited to that employee or teacher."

KRS 161.152 provides: "Each district board of education **may allow** each person employed as a full-time employee in the public schools **not to exceed** three (3) emergency days per school year" and that emergency leave is to be used for "reasons designated by the district board of education." KRS 161.154 provides that "[e]ach district board of education **may** provide **up to** three (3) personal leave days per school year." KRS 160.291 authorizes fringe benefit payments by local boards of education which are deemed to be for services rendered for the benefit of the common schools.

In summary, it is the authority in KRS 161.155(2), allowing a school district to provide more than 10 sick days annually, that allows for the "rollover" of other leave to sick leave. That is, through board policies, some local school districts provide for sick leave in excess of 10 days annually, or 10 sick leave days plus the personal and/or emergency leave not used during the previous school year.

Board policies can be found here: https://policy.ksba.org/. Policies 03.1231 and 03.1236 address the "rollover" of personal and emergency leave to sick leave under the heading "Accumulation." You will see that not all districts provide for this rollover. For example, most districts do not provide for any rollover of emergency leave to sick leave.

Identification of Benchmarks

When I answered the question about benchmarks at the PPOB meeting I was thinking of the Aon policy index that measures TRS against other public pension plans rather than the total plan policy benchmark. Benchmarks are adopted by the TRS board pursuant to law. The board sets these benchmarks based on the recommendations by investment staff in consultation with Aon using accepted practice and recognized market indexes.

Within the total plan policy benchmark for the Retirement Annuity Trust, asset classes are given weights through individual benchmarks, including one for private equity. The current benchmark for private equity is the S&P 500 stock index plus three percentage points. This was a measure adopted years ago in the infancy of TRS's private equity investments. This benchmark has shown over time to be skewed for a couple of reasons. First, no market index exists for private equity as it does for public equity. Also, the reporting data with private equity markets lags the indications seen in public market indexes. Because private equity is an investment in ongoing business enterprises, the value of those business enterprises takes longer to assess and be indicated in returns. As such, the value of the business enterprise in a given quarter may more closely relate to a prior quarter or quarters of a public index. Public indexes also are more volatile than private equity. In light of these factors, this current benchmark sets a virtually unattainable standard anytime the stock market is doing well. For example, as presented to the PPOB in April, TRS ranked in the top 5% in the nation for the 2023 calendar year but was still underperforming its total plan policy benchmark.

This contradiction of top-level performance compared to peers while falling short of − or just meeting − the total plan policy benchmark, is shown in Aon's report for the March 31 quarter:

| Quarter | 1 Year | 3 Years | 5 Years | 7 Years | 10 Years |
|---|---|---|---|---|---|
| Return | 5.2% | 15.3% | 5.1% | 9.1% | 8.3% |
| Benchmark | 5.4% | 16.4% | 6.4% | 9.1% | 8.3% |
| Aon Rank | Top 8% | Top 7% | Top 42% | Top 11% | Top 9% |

TRS annually reviews asset allocations and benchmarks for the upcoming fiscal year. TRS has reevaluated its private equity benchmark in light of the issues described above and a change will be recommended to the Investment Committee.