

1 AN ACT relating to the fiduciary duties owed to the state-administered retirement
2 systems.

3 ***Be it enacted by the General Assembly of the Commonwealth of Kentucky:***

4 ➔Section 1. KRS 21.450 is amended to read as follows:

5 (1) The benefits provided by KRS 21.350 to 21.510 to be paid shall be funded through
6 contract with a reputable life insurance company authorized to do business in this
7 state, or through investment and reinvestment of funds in securities which, at the
8 time of making the investment, are by law permitted for the investment of funds by
9 fiduciaries in this state, or through a combination of such methods. To the extent
10 that funding is provided through insurance contract, no contributions, payments or
11 premiums shall be subject to any tax on insurance premiums or annuity
12 considerations. The investment committee for the judicial retirement fund shall be
13 trustee of any and all funds contributed or appropriated to the retirement system,
14 and shall have sole authority to make insurance contracts or investments.

15 (2) **(a) For the purposes of this subsection:**

16 **1. "Solely in the interest of the members and beneficiaries" shall be**
17 **determined using only pecuniary factors and shall not include any**
18 **purpose to further a nonpecuniary interest;**

19 **2. "Pecuniary factor" means a consideration having a direct and**
20 **material connection to the financial risk or financial return of an**
21 **investment;**

22 **3. A "material connection" is established if there is a substantial**
23 **likelihood that a reasonable investor would consider it important in**
24 **determining the financial risk or the financial return of an**
25 **investment; and**

26 **4. "Nonpecuniary interest" includes an environmental, social, political,**
27 **or ideological interest.**

1 **(b)** The board members, ~~or~~ any investment **manager**, adviser, **or consultant**
2 shall discharge their duties with respect to the funds of the retirement system
3 solely in the interest of the members and beneficiaries and:

4 ~~1.(a)~~ For the exclusive purposes of providing benefits to members and
5 their beneficiaries and defraying reasonable expenses of administering
6 the plan;

7 ~~2.(b)~~ With the care, skill, prudence, and diligence under the
8 circumstances then prevailing that a prudent **person**~~man~~ acting in a
9 like capacity and familiar with such matters would use in the conduct of
10 an enterprise of a like character and with like aims; and

11 ~~3.(c)~~ In accordance with the laws, regulations and other instruments
12 governing the funds.

13 **(c) Evidence that a fiduciary has considered or acted on a nonpecuniary**
14 **interest shall include but is not limited to:**

- 15 **1. Statements, explanations, reports, or correspondence;**
- 16 **2. Communications with portfolio companies;**
- 17 **3. Statements of principles or policies, whether made individually or**
18 **jointly;**
- 19 **4. Votes of shares or proxies; or**
- 20 **5. Coalitions, initiatives, agreements, or commitments to which the**
21 **fiduciary is a participant, affiliate, or signatory.**

22 (3) Any accrual of benefits provided under this or any other applicable statute shall be
23 no less than the benefit adjustment provided for in KRS 21.405(4) from the date of
24 the last establishment of that benefit.

25 (4) The board shall establish ethics policies and procedures by promulgation of
26 administrative regulations in accordance with the provisions of KRS Chapter 13A.
27 The ethics policies shall include but not be limited to annual financial and conflict

1 of interest disclosure requirements which must be completed by all board members
2 and made available to the public upon request.

3 ➔Section 2. KRS 61.650 is amended to read as follows:

4 (1) (a) The board shall be the trustee of funds created by KRS 16.510, 61.515, and
5 61.701 pertaining to the accounts for the Kentucky Employees Retirement
6 System or State Police Retirement System, notwithstanding the provisions of
7 any other statute to the contrary, and shall have exclusive power to invest and
8 reinvest such assets in accordance with federal law.

9 (b) 1. The board shall establish an investment committee whose membership
10 shall be composed of the following:

11 a. The three (3) trustees of the Kentucky Retirement Systems board
12 appointed by the Governor pursuant to KRS 61.645 who have
13 investment experience; and

14 b. Additional trustees appointed by the board chair.

15 2. The investment committee shall have authority to implement the
16 investment policies adopted by the board and act on behalf of the board
17 on all investment-related matters and to acquire, sell, safeguard,
18 monitor, and manage the assets and securities of the several funds.

19 (c) **1. For the purposes of this paragraph:**

20 **a. "Solely in the interest of the members and beneficiaries" shall**
21 **be determined using only pecuniary factors and shall not include**
22 **any purpose to further a nonpecuniary interest;**

23 **b. "Pecuniary factor" means a consideration having a direct and**
24 **material connection to the financial risk or financial return of**
25 **an investment;**

26 **c. A "material connection" is established if there is a substantial**
27 **likelihood that a reasonable investor would consider it important**

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in determining the financial risk or the financial return of an investment; and

d. "Nonpecuniary interest" includes an environmental, social, political, or ideological interest.

2. A trustee, officer, employee, employee of the Kentucky Public Pensions Authority, *investment manager, adviser, or consultant,* or other fiduciary shall discharge duties with respect to the retirement system:

a[1]. Solely in the interest of the members and beneficiaries;

b[2]. For the exclusive purpose of providing benefits to members and beneficiaries and paying reasonable expenses of administering the system;

c[3]. With the care, skill, and caution under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with those matters would use in the conduct of an activity of like character and purpose;

d[4]. Impartially, taking into account any differing interests of members and beneficiaries;

e[5]. Incurring any costs that are appropriate and reasonable; and

f[6]. In accordance with a good-faith interpretation of the law governing the retirement system.

3. *Evidence that a fiduciary has considered or acted on a nonpecuniary interest shall include but is not limited to:*

a. Statements, explanations, reports, or correspondence;

b. Communications with portfolio companies;

c. Statements of principles or policies, whether made individually or jointly;

d. Votes of shares or proxies; or

1 *e. Coalitions, initiatives, agreements, or commitments to which the*
2 *fiduciary is a participant, affiliate, or signatory.*

- 3 (d) In addition to the standards of conduct prescribed by paragraph (c) of this
4 subsection:
- 5 1. All internal investment staff of the Kentucky Public Pensions Authority,
6 and investment consultants shall adhere to the Code of Ethics and
7 Standards of Professional Conduct, and all board trustees shall adhere to
8 the Code of Conduct for Members of a Pension Scheme Governing
9 Body. All codes cited in this subparagraph are promulgated by the CFA
10 Institute; and
 - 11 2. Investment managers shall comply with all applicable provisions of the
12 federal Investment Advisers Act of 1940, as amended, and the rules and
13 regulations promulgated thereunder, and shall comply with all other
14 applicable federal securities statutes and related rules and regulations
15 that apply to investment managers.
- 16 (2) The board, through adopted written policies, shall maintain ownership and control
17 over its assets held in its unitized managed custodial account.
- 18 (3) The board, in keeping with its responsibility as trustee and wherever consistent with
19 its fiduciary responsibilities, shall give priority to the investment of funds in
20 obligation calculated to improve the industrial development and enhance the
21 economic welfare of the Commonwealth.
- 22 (4) The contents of real estate appraisals, engineering or feasibility estimates, and
23 evaluations made by or for the system relative to the acquisition or disposition of
24 property, until such time as all of the property has been acquired or sold, shall be
25 excluded from the application of KRS 61.870 to 61.884 and shall be subject to
26 inspection only upon order of a court of competent jurisdiction.
- 27 (5) Based upon market value at the time of purchase, the board shall limit the amount

1 of assets managed by any one (1) active or passive investment manager to fifteen
2 percent (15%) of the assets in the pension and insurance funds.

3 (6) All contracts for the investment or management of assets of the systems shall not be
4 subject to KRS Chapters 45, 45A, 56, and 57. Instead, the board shall conduct the
5 following process to develop and adopt an investment procurement policy with
6 which all prospective contracts for the investment or management of assets of the
7 systems shall comply:

8 (a) On or before July 1, 2017, the board shall consult with the secretary of the
9 Finance and Administration Cabinet or his or her designee to develop an
10 investment procurement policy, which shall be written to meet best practices
11 in investment management procurement;

12 (b) Thirty (30) days prior to adoption, the board shall tender the preliminary
13 investment procurement policy to the secretary of the Finance and
14 Administration Cabinet or his or her designee for review and comment;

15 (c) Upon receipt of comments from the secretary of the Finance and
16 Administration Cabinet or his or her designee, the board shall choose to adopt
17 or not adopt any recommended changes;

18 (d) Upon adoption, the board shall tender the final investment procurement policy
19 to the secretary of the Finance and Administration Cabinet or his or her
20 designee;

21 (e) No later than thirty (30) days after receipt of the investment procurement
22 policy, the secretary or his or her designee shall certify whether the board's
23 investment procurement policy meets or does not meet best practices for
24 investment management procurement; and

25 (f) Any amendments to the investment procurement policy shall adhere to the
26 requirements set forth by paragraphs (b) to (e) of this subsection.

27 ➔Section 3. KRS 78.790 is amended to read as follows:

- 1 (1) (a) The board shall be the trustee of funds pertaining to the County Employees
2 Retirement System created by KRS 78.510 to 78.852, and KRS 61.701, and
3 shall have full and exclusive power to invest and reinvest such assets in
4 accordance with federal law.
- 5 (b) 1. The board shall establish an investment committee that shall include
6 members of the board with investment experience, elected members, or
7 other members as determined by the board chair, and may also include
8 nonvoting members who have investment expertise.
- 9 2. The investment committee shall have authority to implement the
10 investment policies adopted by the board and act on behalf of the board
11 on all investment-related matters.
- 12 (c) 1. For the purposes of this paragraph:
- 13 a. "Solely in the interest of the members and beneficiaries" shall
14 be determined using only pecuniary factors and shall not include
15 any purpose to further a nonpecuniary interest;
- 16 b. "Pecuniary factor" means a consideration having a direct and
17 material connection to the financial risk or financial return of
18 an investment;
- 19 c. A "material connection" is established if there is a substantial
20 likelihood that a reasonable investor would consider it important
21 in determining the financial risk or the financial return of an
22 investment; and
- 23 d. "Nonpecuniary interest" includes an environmental, social,
24 political, or ideological interest.
- 25 2. A trustee, officer, employee, employee of the Kentucky Public Pensions
26 Authority, investment manager, adviser, consultant, or other fiduciary
27 shall discharge duties with respect to the system:

- 1 a[1]. Solely in the interest of the members and beneficiaries;
- 2 b[2]. For the exclusive purpose of providing benefits to members and
- 3 beneficiaries and paying reasonable expenses of administering the
- 4 system;
- 5 c[3]. With the care, skill, and caution under the circumstances then
- 6 prevailing that a prudent person acting in a like capacity and
- 7 familiar with those matters would use in the conduct of an activity
- 8 of like character and purpose;
- 9 d[4]. Impartially, taking into account any differing interests of members
- 10 and beneficiaries;
- 11 e[5]. Incurring any costs that are appropriate and reasonable; and
- 12 f[6]. In accordance with a good-faith interpretation of the and common
- 13 law governing the system.

14 **3. Evidence that a fiduciary has considered or acted on a nonpecuniary**
 15 **interest shall include but is not limited to:**

- 16 **a. Statements, explanations, reports, or correspondence;**
- 17 **b. Communications with portfolio companies;**
- 18 **c. Statements of principles or policies, whether made individually**
 19 **or jointly;**
- 20 **d. Votes of shares or proxies; or**
- 21 **e. Coalitions, initiatives, agreements, or commitments to which the**
 22 **fiduciary is a participant, affiliate, or signatory.**

23 (d) In addition to the standards of conduct prescribed by paragraph (c) of this
 24 subsection:

- 25 1. All internal investment staff of the Kentucky Public Pensions Authority,
- 26 and investment consultants shall adhere to the Code of Ethics and
- 27 Standards of Professional Conduct, and all board trustees shall adhere to

- 1 the Code of Conduct for Members of a Pension Scheme Governing
2 Body. All codes cited in this subparagraph are promulgated by the CFA
3 Institute; and
- 4 2. Investment managers shall comply with all applicable provisions of the
5 federal Investment Advisers Act of 1940, as amended, and the rules and
6 regulations promulgated thereunder, and shall comply with all other
7 applicable federal securities statutes and related rules and regulations
8 that apply to investment managers.
- 9 (2) The board, through adopted written policies, shall maintain ownership and control
10 over its assets held in its unitized managed custodial account.
- 11 (3) The board, in keeping with its responsibility as the trustee and wherever feasible,
12 shall give priority to the investment of funds in obligations calculated to improve
13 the industrial development and enhance the economic welfare of the
14 Commonwealth.
- 15 (4) The contents of real estate appraisals, engineering or feasibility estimates, and
16 evaluations made by or for the system relative to the acquisition or disposition of
17 property, until such time as all of the property has been acquired or sold, shall be
18 excluded from the application of KRS 61.870 to 61.884 and shall be subject to
19 inspection only upon order of a court of competent jurisdiction.
- 20 (5) Based upon market value at the time of purchase, the board shall limit the amount
21 of assets managed by any one (1) active or passive investment manager to fifteen
22 percent (15%) of the assets in the pension and insurance funds.
- 23 (6) All contracts for the investment or management of assets of the system shall not be
24 subject to KRS Chapters 45, 45A, 56, and 57. Instead, the board shall conduct the
25 following process to develop and adopt an investment procurement policy with
26 which all prospective contracts for the investment or management of assets of the
27 system shall comply:

- 1 (a) The board shall consult with the secretary of the Finance and Administration
2 Cabinet or his or her designee to develop an investment procurement policy,
3 which shall be written to meet best practices in investment management
4 procurement;
- 5 (b) Thirty (30) days prior to adoption, the board shall tender the preliminary
6 investment procurement policy to the secretary of the Finance and
7 Administration Cabinet or his or her designee for review and comment;
- 8 (c) Upon receipt of comments from the secretary of the Finance and
9 Administration Cabinet or his or her designee, the board shall choose to adopt
10 or not adopt any recommended changes;
- 11 (d) Upon adoption, the board shall tender the final investment procurement policy
12 to the secretary of the Finance and Administration Cabinet or his or her
13 designee;
- 14 (e) No later than thirty (30) days after receipt of the investment procurement
15 policy, the secretary or his or her designee shall certify whether the board's
16 investment procurement policy meets or does not meet best practices for
17 investment management procurement; and
- 18 (f) Any amendments to the investment procurement policy shall adhere to the
19 requirements set forth by paragraphs (b) to (e) of this subsection.

20 ➔Section 4. KRS 161.430 is amended to read as follows:

- 21 (1) (a) The board of trustees shall be the trustee of the funds of the retirement system
22 and shall have full power and responsibility for the purchase, sale, exchange,
23 transfer, or other disposition of the investments and moneys of the retirement
24 system. The board shall, by administrative regulation, establish investment
25 policies and procedures to carry out their responsibilities.
- 26 (b) 1. The board shall contract with experienced competent investment
27 managers to invest and manage assets of the system. The board may also

- 1 employ qualified investment staff to advise it on investment matters and
2 to invest and manage assets of the system not to exceed fifty percent
3 (50%) of the system's assets. The board may contract with one (1) or
4 more general investment consultants, as well as specialized investment
5 consultants, to advise it on investment matters.
- 6 2. All internal investment staff and investment consultants shall adhere to
7 the Code of Ethics and Standards of Professional Conduct, and all board
8 trustees shall adhere to the Code of Conduct for Members of a Pension
9 Scheme Governing Body, promulgated by the CFA Institute. Investment
10 managers shall comply with the federal Investment Advisers Act of
11 1940, as amended, and the rules and regulations promulgated thereunder
12 and shall comply with all other applicable federal securities statutes and
13 related rules and regulations that apply to investment managers.
- 14 3. No investment manager shall manage more than forty percent (40%) of
15 the funds of the retirement system.
- 16 (c) The board may appoint an investment committee to act for the board in all
17 matters of investment, subject to the approval of the board of trustees. The
18 board of trustees, in keeping with their responsibilities as trustees and
19 wherever consistent with their fiduciary responsibilities, shall give priority to
20 the investment of funds in obligations calculated to improve the industrial
21 development and enhance the economic welfare of the Commonwealth.
22 Toward this end, the board shall develop procedures for informing the
23 business community of the potential for in-state investments by the retirement
24 fund, accepting and evaluating applications for the in-state investment of
25 funds, and working with members of the business community in executing in-
26 state investments which are consistent with the board's fiduciary
27 responsibilities. The board shall include in the criteria it uses to evaluate in-

1 state investments their potential for creating new employment opportunities
 2 and adding to the total job pool in Kentucky. The board may cooperate with
 3 the board of trustees of Kentucky Retirement Systems in developing its
 4 program and procedures, and shall report to the Legislative Research
 5 Commission annually on its progress in placing in-state investments. The first
 6 report shall be submitted by October 1, 1991, and subsequent reports shall be
 7 submitted by October 1 of each year thereafter. The report shall include the
 8 number of applications for in-state investment received, the nature of the
 9 investments proposed, the amount requested, the amount invested, and the
 10 percentage of applications which resulted in investments.

11 (2) **(a) For the purposes of this subsection:**

12 **1. "Solely in the interest of the members and beneficiaries" shall be**
 13 **determined using only pecuniary factors and shall not include any**
 14 **purpose to further a nonpecuniary interest;**

15 **2. "Pecuniary factor" means a consideration having a direct and**
 16 **material connection to the financial risk or financial return of an**
 17 **investment;**

18 **3. A "material connection" is established if there is a substantial**
 19 **likelihood that a reasonable investor would consider it important in**
 20 **determining the financial risk or the financial return of an**
 21 **investment; and**

22 **4. "Nonpecuniary interest" includes an environmental, social, political,**
 23 **or ideological interest.**

24 **(b)** The board members, ~~and~~ investment **managers, advisers, or** consultants
 25 shall discharge their duties with respect to the assets of the system solely in
 26 the interests of the active contributing members and annuitants and:

27 **1. ~~(a)~~** For the exclusive purpose of providing benefits to members and

1 annuitants and defraying reasonable expenses of administering the
2 system;

3 ~~2.[(b)]~~ With the care, skill, prudence, and diligence under the
4 circumstances then prevailing that a prudent person acting in a like
5 capacity and familiar with these matters would use in the conduct of an
6 enterprise of a like character and with like aims;

7 ~~3.[(e)]~~ By diversifying the investments of the plan so as to minimize the
8 risk of large losses, unless under the circumstances it is clearly prudent
9 not to do so; and

10 ~~4.[(d)]~~ In accordance with the laws, administrative regulations, and other
11 instruments governing the system.

12 **(c) Evidence that a fiduciary has considered or acted on a nonpecuniary**
13 **interest shall include but is not limited to:**

14 **1. Statements, explanations, reports, or correspondence;**

15 **2. Communications with portfolio companies;**

16 **3. Statements of principles or policies, whether made individually or**
17 **jointly;**

18 **4. Votes of shares or proxies; or**

19 **5. Coalitions, initiatives, agreements, or commitments to which the**
20 **fiduciary is a participant, affiliate, or signatory.**

21 (3) (a) In choosing and contracting for professional investment management and
22 consulting services, the board shall do so prudently and in the interest of the
23 members and annuitants. Any contract that the board makes with an
24 investment manager shall set forth policies and guidelines of the board with
25 reference to standard rating services and specific criteria for determining the
26 quality of investments. Expenses directly related to investment management
27 and consulting services shall be financed from the guarantee fund in amounts

1 approved by the board.

2 (b) An investment manager or consultant appointed under this section shall
3 acknowledge in writing his or her fiduciary responsibilities to the fund. To be
4 eligible for appointment, an investment manager, consultant, or an affiliate,
5 shall be:

6 1. Registered under the Federal Investment Advisers Act of 1940; or

7 2. A bank as defined by that Act; or

8 3. An insurance company qualified to perform investment services under
9 the laws of more than one (1) state.

10 (4) No investment or disbursement of funds shall be made unless authorized by the
11 board of trustees, except that the board, in order to ensure timely market
12 transactions, shall establish investment guidelines and may permit its staff and
13 investment managers who are employed or under contract with the board pursuant
14 to this section to execute purchases and sales of investment instruments within
15 those guidelines without prior board approval.

16 (5) In discharging his or her administrative duties under this section, a trustee shall
17 strive to administer the retirement system in an efficient and cost-effective manner
18 for the taxpayers of the Commonwealth of Kentucky.

19 (6) Notwithstanding any other provision of KRS 161.220 to 161.716, no funds of the
20 Teachers' Retirement System, including fees and commissions paid to an
21 investment manager, private fund, or company issuing securities, who manages
22 systems assets, shall be used to pay fees and commissions to placement agents. For
23 purposes of this subsection, "placement agent" means a third-party individual, who
24 is not an employee, or firm, wholly or partially owned by the entity being hired,
25 who solicits investments on behalf of an investment manager, private fund, or
26 company issuing securities.

27 (7) All contracts for the investment or management of assets of the system shall not be

1 subject to KRS Chapters 45, 45A, 56, and 57. Instead, the board shall conduct the
2 following process to develop and adopt an investment procurement policy with
3 which all prospective contracts for the investment or management of assets of the
4 system shall comply:

- 5 (a) On or before July 1, 2017, the board shall consult with the secretary of the
6 Finance and Administration Cabinet or his or her designee to develop an
7 investment procurement policy, which shall be written to meet best practices
8 in investment management procurement;
- 9 (b) Thirty (30) days prior to adoption, the board shall tender the preliminary
10 investment procurement policy to the secretary of the Finance and
11 Administration Cabinet or his or her designee for review and comment;
- 12 (c) Upon receipt of comments from the secretary of the Finance and
13 Administration Cabinet or his or her designee, the board shall choose to adopt
14 or not adopt any recommended changes;
- 15 (d) Upon adoption, the board shall tender the final investment procurement policy
16 to the secretary of the Finance and Administration Cabinet or his or her
17 designee;
- 18 (e) No later than thirty (30) days after receipt of the investment procurement
19 policy, the secretary or his or her designee shall certify whether the board's
20 investment procurement policy meets or does not meet best practices for
21 investment management procurement; and
- 22 (f) Any amendments to the investment procurement policy shall adhere to the
23 requirements set forth by paragraphs (b) to (e) of this subsection.