

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 material
20 connection to the financial risk or financial return of an investment;
- 21 3. A "material connection" is established if there is a substantial likelihood
22 that a reasonable investor would consider it important in determining the
23 financial risk or the financial return of an investment;
- 24 4. "Nonpecuniary interest" includes but is not limited to an environmental,
25 social, political, or ideological interest which does not have a direct and
26 material connection to the financial risk or financial return of an
27 investment;~~and~~

- 1 5. "Investment manager" shall have the same definition attributed to
2 "investment adviser" under the federal Investment Advisers Act of 1940,
3 15 U.S.C. sec. 80b-2;
- 4 6. "Shareholder-sponsored proposal" means a proposal by a shareholder
5 included in the proxy statement of an issuer of securities pursuant to
6 17 C.F.R. sec. 240.14a-8;
- 7 7. "Economic analysis" means a written analysis of the economic impact
8 of a shareholder-sponsored proposal, which shall include, at a
9 minimum:
- 10 a. The subject matter of the shareholder-sponsored proposal;
11 b. Whether the board of directors of the issuer of securities opposes
12 the shareholder-sponsored proposal and the stated reasons for
13 the opposition;
14 c. Whether the shareholder-sponsored proposal is consistent with
15 the investment policy of the retirement system;
16 d. The economic benefits and costs of implementing the
17 shareholder-sponsored proposal, as written, in the long and
18 short term;
19 e. The quantifiable impact of the shareholder-sponsored proposal,
20 as written, on the investment returns of the funds of the
21 retirement system; and
22 f. An explanation of the modeling, procedures, and processes used
23 to complete the economic analysis; and
- 24 8. a. "Proxy adviser" means any person who is engaged in the
25 business of providing advice, research, analysis, ratings, or
26 recommendations specifically with respect to proxy voting and
27 who has entered into an agreement or contracted with the board

1 of trustees of the retirement system to receive compensation for
2 those purposes.

3 b. "Proxy adviser" does not include an investment manager as
4 defined in this paragraph.

5 (b) The board members, any investment manager or other fiduciary, or proxy
6 adviser shall discharge their duties with respect to the funds of the retirement
7 system solely in the interest of the members and beneficiaries and:

- 8 1. For the exclusive purposes of providing benefits to members and their
9 beneficiaries and defraying reasonable expenses of administering the
10 plan;
- 11 2. With the care, skill, prudence, and diligence under the circumstances
12 then prevailing that a prudent person acting in a like capacity and
13 familiar with such matters would use in the conduct of an enterprise of a
14 like character and with like aims; and
- 15 3. In accordance with the federal, state, and common laws, regulations and
16 other instruments governing the funds and fiduciaries.

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

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

26 (d) When exercising or recommending a vote on a shareholder-sponsored
27 proposal, a proxy adviser that has entered into an agreement or contracted

1 with the board of trustees of the retirement system acts solely in the interest
 2 of the members and beneficiaries under this subsection if:

3 1. The proxy adviser's vote or recommendation is consistent with the
 4 recommendation of the board of directors of the issuer of the shares,
 5 provided:

6 a. The board of directors of the issuer of the shares is composed of
 7 a majority of independent directors; and

8 b. The recommendation of the board of directors is not for the
 9 purpose of furthering a nonpecuniary interest; or

10 2. The proxy adviser's vote or recommendation is inconsistent with the
 11 recommendation of the board of directors of the issuer of the shares,
 12 provided the proxy adviser conducts and documents an economic
 13 analysis demonstrating that the vote or recommendation is solely in
 14 the interest of the members and beneficiaries.

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

18 (4) The board shall establish ethics policies and procedures by promulgation of
 19 administrative regulations in accordance with the provisions of KRS Chapter 13A.
 20 The ethics policies shall include but not be limited to annual financial and conflict
 21 of interest disclosure requirements which must be completed by all board members
 22 and made available to the public upon request.

23 (5) In addition to the standards of conduct prescribed by subsection (2) of this section:

24 (a) Investment managers shall comply with all applicable provisions of the
 25 Investment Advisers Act of 1940, as amended, and the rules and regulations
 26 promulgated thereunder, and shall comply with all other applicable federal
 27 securities statutes and related rules and regulations that apply to investment

1 managers; and

2 (b) Proxy advisers and proxy voting services shall comply with all applicable
3 provisions of the Investment Advisers Act of 1940, as amended, and the rules
4 and regulations promulgated thereunder, and shall comply with all other
5 federal statutes and related rules and regulations that apply to proxy advisers
6 and proxy voting services.

7 (6) No contract or agreement, whether made in writing or not, shall in any manner
8 waive, restrict, or limit a fiduciary's liability as to any of the duties imposed by this
9 section. Any agreement shall specify that it is made in the Commonwealth *of*
10 *Kentucky* and governed by the laws of the Commonwealth *of Kentucky*.

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

12 (1) (a) The board shall be the trustee of funds created by KRS 16.510, 61.515, and
13 61.701 pertaining to the accounts for the Kentucky Employees Retirement
14 System or State Police Retirement System, notwithstanding the provisions of
15 any other statute to the contrary, and shall have exclusive power to invest and
16 reinvest such assets in accordance with federal law.

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

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

22 b. Additional trustees appointed by the board chair.

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

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

- 1 a. "Solely in the interest of the members and beneficiaries" shall be
2 determined using only pecuniary factors and shall not include any
3 purpose to further a nonpecuniary interest;
- 4 b. "Pecuniary factor" means a consideration having a direct and
5 material connection to the financial risk or financial return of an
6 investment;
- 7 c. A "material connection" is established if there is a substantial
8 likelihood that a reasonable investor would consider it important in
9 determining the financial risk or the financial return of an
10 investment;
- 11 d. "Nonpecuniary interest" includes but is not limited to an
12 environmental, social, political, or ideological interest which does
13 not have a direct and material connection to the financial risk or
14 financial return of an investment;~~and~~
- 15 e. "Investment manager" shall have the same definition attributed to
16 "investment adviser" under the federal Investment Advisers Act of
17 1940, 15 U.S.C. sec. 80b-2;
- 18 **f. "Shareholder-sponsored proposal" means a proposal by a**
19 **shareholder included in the proxy statement of an issuer of**
20 **securities pursuant to 17 C.F.R. sec. 240.14a-8;**
- 21 **g. "Economic analysis" means a written analysis of the economic**
22 **impact of a shareholder-sponsored proposal, which shall**
23 **include, at a minimum:**
- 24 **i. The subject matter of the shareholder-sponsored proposal;**
25 **ii. Whether the board of directors of the issuer of securities**
26 **opposes the shareholder-sponsored proposal and the stated**
27 **reasons for the opposition;**

- 1 iii. Whether the shareholder-sponsored proposal is consistent
 2 with the investment policy of the retirement systems;
 3 iv. The economic benefits and costs of implementing the
 4 shareholder-sponsored proposal, as written, in the long and
 5 short term;
 6 v. The quantifiable impact of the shareholder-sponsored
 7 proposal, as written, on the investment returns of the funds
 8 of the retirement systems; and
 9 vi. An explanation of the modeling, procedures, and processes
 10 used to complete the economic analysis; and
 11 h. i. "Proxy adviser" means any person who is engaged in the
 12 business of providing advice, research, analysis, ratings, or
 13 recommendations specifically with respect to proxy voting
 14 and who has entered into an agreement or contracted with
 15 the board of trustees of the retirement system to receive
 16 compensation for those purposes.
 17 ii "Proxy adviser" does not include an investment manager
 18 as defined in this subparagraph.
 19 2. A trustee, officer, employee, employee of the Kentucky Public Pensions
 20 Authority, investment manager, or other fiduciary, or proxy adviser shall
 21 discharge duties with respect to the retirement system:
 22 a. Solely in the interest of the members and beneficiaries;
 23 b. For the exclusive purpose of providing benefits to members and
 24 beneficiaries and paying reasonable expenses of administering the
 25 system;
 26 c. With the care, skill, and caution under the circumstances then
 27 prevailing that a prudent person acting in a like capacity and

- 1 familiar with those matters would use in the conduct of an activity
2 of like character and purpose;
- 3 d. Impartially, taking into account any differing interests of members
4 and beneficiaries;
- 5 e. Incurring any costs that are appropriate and reasonable; and
6 f. In accordance with a good-faith interpretation of the federal, state,
7 and common law governing the system and fiduciaries.

- 8 3. Evidence that a fiduciary has considered or acted on a nonpecuniary
9 interest shall include but is not limited to:
- 10 a. Statements, explanations, reports, or correspondence;
11 b. Communications with portfolio companies;
12 c. Statements of principles or policies, whether made individually or
13 jointly;
14 d. Votes of shares or proxies; or
15 e. Coalitions, initiatives, agreements, or commitments to which the
16 fiduciary is a participant, affiliate, or signatory.

17 **4. When exercising or recommending a vote on a shareholder-sponsored**
18 **proposal, a proxy adviser that has entered into an agreement or**
19 **contracted with the board of trustees of the retirement system acts**
20 **solely in the interest of the members and beneficiaries under this**
21 **subsection if:**

22 **a. The proxy adviser's vote or recommendation is consistent with**
23 **the recommendation of the board of directors of the issuer of the**
24 **shares, provided:**

25 **i. The board of directors of the issuer of the shares is**
26 **composed of a majority of independent directors; and**

27 **ii. The recommendation of the board of directors is not for the**

1 purpose of furthering a nonpecuniary interest; or
2 b. The proxy adviser's vote or recommendation is inconsistent with
3 the recommendation of the board of directors of the issuer of the
4 shares, provided the proxy adviser conducts and documents an
5 economic analysis demonstrating that the vote or
6 recommendation is solely in the interest of the members and
7 beneficiaries.

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

- 10 1. All internal investment staff of the Kentucky Public Pensions Authority,
11 and investment consultants shall adhere to the Code of Ethics and
12 Standards of Professional Conduct, and all board trustees shall adhere to
13 the Code of Conduct for Members of a Pension Scheme Governing
14 Body. All codes cited in this subparagraph are promulgated by the CFA
15 Institute;
- 16 2. Investment managers shall comply with all applicable provisions of the
17 federal Investment Advisers Act of 1940, as amended, and the rules and
18 regulations promulgated thereunder, and shall comply with all other
19 applicable federal securities statutes and related rules and regulations
20 that apply to investment managers; and
- 21 3. Proxy advisers and proxy voting services shall comply with all
22 applicable provisions of the Investment Advisers Act of 1940, as
23 amended, and the rules and regulations promulgated thereunder, and
24 shall comply with all other federal statutes and related rules and
25 regulations that apply to proxy advisers and proxy voting services.

26 (e) No contract or agreement, whether made in writing or not, shall in any
27 manner waive, restrict, or limit a fiduciary's liability as to any of the duties

1 imposed by this section. Any agreement shall specify that it is made in the
2 Commonwealth of Kentucky and governed by the laws of the Commonwealth
3 of Kentucky.

- 4 (2) The board, through adopted written policies, shall maintain ownership and control
5 over its assets held in its unitized managed custodial account.
- 6 (3) The board, in keeping with its responsibility as trustee and wherever consistent with
7 its fiduciary responsibilities, shall give priority to the investment of funds in
8 obligation calculated to improve the industrial development and enhance the
9 economic welfare of the Commonwealth.
- 10 (4) The contents of real estate appraisals, engineering or feasibility estimates, and
11 evaluations made by or for the system relative to the acquisition or disposition of
12 property, until such time as all of the property has been acquired or sold, shall be
13 excluded from the application of KRS 61.870 to 61.884 and shall be subject to
14 inspection only upon order of a court of competent jurisdiction.
- 15 (5) Based upon market value at the time of purchase, the board shall limit the amount
16 of assets managed by any one (1) active or passive investment manager to fifteen
17 percent (15%) of the assets in the pension and insurance funds.
- 18 (6) All contracts for the investment or management of assets of the systems shall not be
19 subject to KRS Chapters 45, 45A, 56, and 57. Instead, the board shall conduct the
20 following process to develop and adopt an investment procurement policy with
21 which all prospective contracts for the investment or management of assets of the
22 systems shall comply:
- 23 (a) On or before July 1, 2017, the board shall consult with the secretary of the
24 Finance and Administration Cabinet or his or her designee to develop an
25 investment procurement policy, which shall be written to meet best practices
26 in investment management procurement;
- 27 (b) Thirty (30) days prior to adoption, the board shall tender the preliminary

- 1 investment procurement policy to the secretary of the Finance and
2 Administration Cabinet or his or her designee for review and comment;
- 3 (c) Upon receipt of comments from the secretary of the Finance and
4 Administration Cabinet or his or her designee, the board shall choose to adopt
5 or not adopt any recommended changes;
- 6 (d) Upon adoption, the board shall tender the final investment procurement policy
7 to the secretary of the Finance and Administration Cabinet or his or her
8 designee;
- 9 (e) No later than thirty (30) days after receipt of the investment procurement
10 policy, the secretary or his or her designee shall certify whether the board's
11 investment procurement policy meets or does not meet best practices for
12 investment management procurement; and
- 13 (f) Any amendments to the investment procurement policy shall adhere to the
14 requirements set forth by paragraphs (b) to (e) of this subsection.
- 15 (7) (a) The board shall adopt written proxy voting guidelines which are consistent
16 with the fiduciary duties and other requirements of this section.
- 17 (b) The board shall not adopt the recommendations of a proxy adviser or proxy
18 voting service and shall not allow such proxy adviser or proxy voting service
19 to vote on behalf of the system, unless the proxy adviser or proxy voting
20 service acknowledges in writing and accepts under contract its duties under
21 this section and commits to follow the board-adopted proxy voting guidelines
22 when voting the system's shares in order to comply with the board's fiduciary
23 duties and other responsibilities under this section.
- 24 (c) All shares held by or on behalf of the system, and which the system is entitled
25 to vote under state, federal, or common laws, shall be voted according to the
26 proxy voting guidelines adopted by the board and subject to the fiduciary
27 duties and other requirements of this section by:

- 1 1. The board, the investment committee of the board, or an employee or
2 employees of the Authority who are fiduciaries under subsection (1) of
3 this section and are appointed or otherwise authorized by the board; or
- 4 2. A proxy adviser or proxy voting service that acknowledges in writing
5 and accepts under contract its duties under this section and commits to
6 follow the board-adopted proxy voting guidelines when voting the
7 system's shares in order to comply with the board's fiduciary duties and
8 other responsibilities under this section.

9 (d) All proxy votes shall be reported at least quarterly to the board. For each vote,
10 the report shall provide:

- 11 1. The vote caption;
- 12 2. The date of the vote;
- 13 3. The company's name;
- 14 4. The vote cast for the system;
- 15 5. The recommendation of the company's management; and
- 16 6. If applicable, the recommendation of the proxy adviser or proxy voting
17 service.

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

19 (1) (a) The board shall be the trustee of funds pertaining to the County Employees
20 Retirement System created by KRS 78.510 to 78.852, and KRS 61.701, and
21 shall have full and exclusive power to invest and reinvest such assets in
22 accordance with federal law.

23 (b) 1. The board shall establish an investment committee that shall include
24 members of the board with investment experience, elected members, or
25 other members as determined by the board chair, and may also include
26 nonvoting members who have investment expertise.

27 2. The investment committee shall have authority to implement the

1 investment policies adopted by the board and act on behalf of the board
2 on all investment-related matters.

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

4 a. "Solely in the interest of the members and beneficiaries" shall be
5 determined using only pecuniary factors and shall not include any
6 purpose to further a nonpecuniary interest;

7 b. "Pecuniary factor" means a consideration having a direct and
8 material connection to the financial risk or financial return of an
9 investment;

10 c. A "material connection" is established if there is a substantial
11 likelihood that a reasonable investor would consider it important in
12 determining the financial risk or the financial return of an
13 investment;

14 d. "Nonpecuniary interest" includes but is not limited to an
15 environmental, social, political, or ideological interest which does
16 not have a direct and material connection to the financial risk or
17 financial return of an investment;~~and~~

18 e. "Investment manager" shall have the same definition attributed to
19 "investment adviser" under the federal Investment Advisers Act of
20 1940, 15 U.S.C. sec. 80b-2;

21 **f. "Shareholder-sponsored proposal" means a proposal by a**
22 **shareholder included in the proxy statement of an issuer of**
23 **securities pursuant to 17 C.F.R. sec. 240.14a-8;**

24 **g. "Economic analysis" means a written analysis of the economic**
25 **impact of a shareholder-sponsored proposal, which shall**
26 **include, at a minimum:**

27 **i. The subject matter of the shareholder-sponsored proposal;**

- 1 ii. Whether the board of directors of the issuer of securities
 2 opposes the shareholder-sponsored proposal and the stated
 3 reasons for the opposition;
- 4 iii. Whether the shareholder-sponsored proposal is consistent
 5 with the investment policy of the retirement system;
- 6 iv. The economic benefits and costs of implementing the
 7 shareholder-sponsored proposal, as written, in the long and
 8 short term;
- 9 v. The quantifiable impact of the shareholder-sponsored
 10 proposal, as written, on the investment returns of the funds
 11 of the retirement system; and
- 12 vi. An explanation of the modeling, procedures, and processes
 13 used to complete the economic analysis; and
- 14 h. i "Proxy adviser" means any person who is engaged in the
 15 business of providing advice, research, analysis, ratings, or
 16 recommendations specifically with respect to proxy voting
 17 and who has entered into an agreement or contracted with
 18 the board of trustees of the retirement system to receive
 19 compensation for those purposes.
- 20 ii. "Proxy adviser" does not include an investment manager
 21 as defined in this subparagraph.

- 22 2. A trustee, officer, employee, employee of the Kentucky Public Pensions
 23 Authority, investment manager, or other fiduciary, or proxy adviser shall
 24 discharge duties with respect to the system:
- 25 a. Solely in the interest of the members and beneficiaries;
- 26 b. For the exclusive purpose of providing benefits to members and
 27 beneficiaries and paying reasonable expenses of administering the

- 1 system;
- 2 c. With the care, skill, and caution under the circumstances then
- 3 prevailing that a prudent person acting in a like capacity and
- 4 familiar with those matters would use in the conduct of an activity
- 5 of like character and purpose;
- 6 d. Impartially, taking into account any differing interests of members
- 7 and beneficiaries;
- 8 e. Incurring any costs that are appropriate and reasonable; and
- 9 f. In accordance with a good-faith interpretation of the federal, state,
- 10 and common law governing the system and fiduciaries.
- 11 3. Evidence that a fiduciary has considered or acted on a nonpecuniary
- 12 interest shall include but is not limited to:
- 13 a. Statements, explanations, reports, or correspondence;
- 14 b. Communications with portfolio companies;
- 15 c. Statements of principles or policies, whether made individually or
- 16 jointly;
- 17 d. Votes of shares or proxies; or
- 18 e. Coalitions, initiatives, agreements, or commitments to which the
- 19 fiduciary is a participant, affiliate, or signatory.
- 20 **4. When exercising or recommending a vote on a shareholder-sponsored**
- 21 **proposal, a proxy adviser that has entered into an agreement or**
- 22 **contracted with the board of trustees of the retirement system acts**
- 23 **solely in the interest of the members and beneficiaries under this**
- 24 **subsection if:**
- 25 **a. The proxy adviser's vote or recommendation is consistent with**
- 26 **the recommendation of the board of directors of the issuer of the**
- 27 **shares, provided:**

1 *i. The board of directors of the issuer of the shares is*
2 *composed of a majority of independent directors; and*

3 *ii. The recommendation of the board of directors is not for the*
4 *purpose of furthering a nonpecuniary interest; or*

5 *b. The proxy adviser's vote or recommendation is inconsistent with*
6 *the recommendation of the board of directors of the issuer of the*
7 *shares, provided the proxy adviser conducts and documents an*
8 *economic analysis demonstrating that the vote or*
9 *recommendation is solely in the interest of the members and*
10 *beneficiaries.*

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

- 13 1. All internal investment staff of the Kentucky Public Pensions Authority,
14 and investment consultants shall adhere to the Code of Ethics and
15 Standards of Professional Conduct, and all board trustees shall adhere to
16 the Code of Conduct for Members of a Pension Scheme Governing
17 Body. All codes cited in this subparagraph are promulgated by the CFA
18 Institute;
- 19 2. Investment managers shall comply with all applicable provisions of the
20 federal Investment Advisers Act of 1940, as amended, and the rules and
21 regulations promulgated thereunder, and shall comply with all other
22 applicable federal securities statutes and related rules and regulations
23 that apply to investment managers; and
- 24 3. Proxy advisers and proxy voting services shall comply with all
25 applicable provisions of the Investment Advisers Act of 1940, as
26 amended, and the rules and regulations promulgated thereunder, and
27 shall comply with all other federal statutes and related rules and

1 regulations that apply to proxy advisers and proxy voting services.

2 (e) No contract or agreement, whether made in writing or not, shall in any
3 manner waive, restrict, or limit a fiduciary's liability as to any of the duties
4 imposed by this section. Any agreement shall specify that it is made in the
5 Commonwealth and governed by the laws of the Commonwealth.

6 (2) The board, through adopted written policies, shall maintain ownership and control
7 over its assets held in its unitized managed custodial account.

8 (3) The board, in keeping with its responsibility as the trustee and wherever feasible,
9 shall give priority to the investment of funds in obligations calculated to improve
10 the industrial development and enhance the economic welfare of the
11 Commonwealth.

12 (4) The contents of real estate appraisals, engineering or feasibility estimates, and
13 evaluations made by or for the system relative to the acquisition or disposition of
14 property, until such time as all of the property has been acquired or sold, shall be
15 excluded from the application of KRS 61.870 to 61.884 and shall be subject to
16 inspection only upon order of a court of competent jurisdiction.

17 (5) Based upon market value at the time of purchase, the board shall limit the amount
18 of assets managed by any one (1) active or passive investment manager to fifteen
19 percent (15%) of the assets in the pension and insurance funds.

20 (6) All contracts for the investment or management of assets of the system shall not be
21 subject to KRS Chapters 45, 45A, 56, and 57. Instead, the board shall conduct the
22 following process to develop and adopt an investment procurement policy with
23 which all prospective contracts for the investment or management of assets of the
24 system shall comply:

25 (a) The board shall consult with the secretary of the Finance and Administration
26 Cabinet or his or her designee to develop an investment procurement policy,
27 which shall be written to meet best practices in investment management

- 1 procurement;
- 2 (b) Thirty (30) days prior to adoption, the board shall tender the preliminary
3 investment procurement policy to the secretary of the Finance and
4 Administration Cabinet or his or her designee for review and comment;
- 5 (c) Upon receipt of comments from the secretary of the Finance and
6 Administration Cabinet or his or her designee, the board shall choose to adopt
7 or not adopt any recommended changes;
- 8 (d) Upon adoption, the board shall tender the final investment procurement policy
9 to the secretary of the Finance and Administration Cabinet or his or her
10 designee;
- 11 (e) No later than thirty (30) days after receipt of the investment procurement
12 policy, the secretary or his or her designee shall certify whether the board's
13 investment procurement policy meets or does not meet best practices for
14 investment management procurement; and
- 15 (f) Any amendments to the investment procurement policy shall adhere to the
16 requirements set forth by paragraphs (b) to (e) of this subsection.
- 17 (7) (a) The board shall adopt written proxy voting guidelines, which are consistent
18 with the fiduciary duties and other requirements of this section.
- 19 (b) The board shall not adopt the recommendations of a proxy adviser or proxy
20 voting service and shall not allow such proxy adviser or proxy voting service
21 to vote on behalf of the system, unless the proxy adviser or proxy voting
22 service acknowledges in writing and accepts under contract its duties under
23 this section and commits to follow the board-adopted proxy voting guidelines
24 when voting the system's shares in order to comply with the board's fiduciary
25 duties and other responsibilities under this section.
- 26 (c) All shares held by or on behalf of the system, and which the system is entitled
27 to vote under state, federal, or common laws, shall be voted according to the

1 proxy voting guidelines adopted by the board and subject to the fiduciary
2 duties and other requirements of this section by:

- 3 1. The board, the investment committee of the board, or an employee or
4 employees of the Authority who are fiduciaries under subsection (1) of
5 this section and are appointed or otherwise authorized by the board; or
- 6 2. A proxy adviser or proxy voting service that acknowledges in writing
7 and accepts under contract its duties under this section and commits to
8 follow the board-adopted proxy voting guidelines when voting the
9 system's shares in order to comply with the board's fiduciary duties and
10 other responsibilities under this section.

11 (d) All proxy votes shall be reported at least quarterly to the board. For each vote,
12 the report shall provide:

- 13 1. The vote caption;
- 14 2. The date of the vote;
- 15 3. The company's name;
- 16 4. The vote cast for the system;
- 17 5. The recommendation of the company's management; and
- 18 6. If applicable, the recommendation of the proxy adviser or proxy voting
19 service.

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 annuitants~~[beneficiaries]~~"
13 shall be determined using only pecuniary factors and shall not include
14 any purpose to further a nonpecuniary interest;
- 15 2. "Pecuniary factor" means a consideration having a direct and material
16 connection to the financial risk or financial return of an investment;
- 17 3. A "material connection" is established if there is a substantial likelihood
18 that a reasonable investor would consider it important in determining the
19 financial risk or the financial return of an investment;
- 20 4. "Nonpecuniary interest" includes but is not limited to an environmental,
21 social, political, or ideological interest which does not have a direct and
22 material connection to the financial risk or financial return of an
23 investment;~~[and]~~
- 24 5. "Investment manager" and "investment consultant" shall have the same
25 definition attributed to "investment adviser" under the federal
26 Investment Advisers Act of 1940, 15 U.S.C. sec. 80b-2;

27 6. *Shareholder-sponsored proposal* means a proposal by a shareholder

1 included in the proxy statement of an issuer of securities pursuant to
2 17 C.F.R. sec. 240.14a-8;

3 7. "Economic analysis" means a written analysis of the economic impact
4 of a shareholder-sponsored proposal, which shall include, at a
5 minimum:

6 a. The subject matter of the shareholder-sponsored proposal;

7 b. Whether the board of directors of the issuer of securities opposes
8 the shareholder-sponsored proposal and the stated reasons for
9 the opposition;

10 c. Whether the shareholder-sponsored proposal is consistent with
11 the investment policy of the retirement system;

12 d. The economic benefits and costs of implementing the
13 shareholder-sponsored proposal, as written, in the long and
14 short term;

15 e. The quantifiable impact of the shareholder-sponsored proposal,
16 as written, on the investment returns of the funds of the
17 retirement system; and

18 f. An explanation of the modeling, procedures, and processes used
19 to complete the economic analysis; and

20 8. a. "Proxy adviser" means any person who is engaged in the
21 business of providing advice, research, analysis, ratings, or
22 recommendations specifically with respect to proxy voting and
23 who has entered into an agreement or contracted with the board
24 of trustees of the retirement system to receive compensation for
25 those purposes.

26 b. "Proxy adviser" does not include an investment manager or
27 investment consultant as defined in this paragraph.

1 (b) The board members, investment managers, investment consultants, or other
2 fiduciaries, and proxy advisers shall discharge their duties with respect to the
3 assets of the system solely in the interests of the active contributing members
4 and annuitants and:

- 5 1. For the exclusive purpose of providing benefits to members and
6 annuitants and defraying reasonable expenses of administering the
7 system;
- 8 2. With the care, skill, prudence, and diligence under the circumstances
9 then prevailing that a prudent person acting in a like capacity and
10 familiar with these matters would use in the conduct of an enterprise of
11 a like character and with like aims;
- 12 3. By diversifying the investments of the plan so as to minimize the risk of
13 large losses, unless under the circumstances it is clearly prudent not to
14 do so; and
- 15 4. In accordance with the federal, state, and common laws, administrative
16 regulations, and other instruments governing the system and fiduciaries.

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

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

26 **(d) When exercising or recommending a vote on a shareholder-sponsored**
27 **proposal, a proxy adviser that has entered into an agreement or contracted**

1 with the board of trustees of the retirement system acts solely in the interest
 2 of the members and annuitants under this subsection if:

3 1. The proxy adviser's vote or recommendation is consistent with the
 4 recommendation of the board of directors of the issuer of the shares,
 5 provided:

6 a. The board of directors of the issuer of the shares is composed of
 7 a majority of independent directors; and

8 b. The recommendation of the board of directors is not for the
 9 purpose of furthering a nonpecuniary interest; or

10 2. The proxy adviser's vote or recommendation is inconsistent with the
 11 recommendation of the board of directors of the issuer of the shares,
 12 provided the proxy adviser conducts and documents an economic
 13 analysis demonstrating that the vote or recommendation is solely in
 14 the interest of the members and annuitants.

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

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

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

- 1 2. A bank as defined by that Act; or
- 2 3. An insurance company qualified to perform investment services under
- 3 the laws of more than one (1) state.
- 4 (c) Proxy advisers and proxy voting services shall comply with all applicable
- 5 provisions of the Investment Advisers Act of 1940, as amended, and the rules
- 6 and regulations promulgated thereunder, and shall comply with all other
- 7 federal statutes and related rules and regulations that apply to proxy advisers
- 8 and proxy voting services.
- 9 (d) No contract or agreement, whether made in writing or not, shall in any
- 10 manner waive, restrict, or limit a fiduciary's liability as to any of the duties
- 11 imposed by this section. Any agreement shall specify that it is made in the
- 12 Commonwealth of Kentucky and governed by the laws of the Commonwealth
- 13 of Kentucky.
- 14 (4) No investment or disbursement of funds shall be made unless authorized by the
- 15 board of trustees, except that the board, in order to ensure timely market
- 16 transactions, shall establish investment guidelines and may permit its staff and
- 17 investment managers who are employed or under contract with the board pursuant
- 18 to this section to execute purchases and sales of investment instruments within
- 19 those guidelines without prior board approval.
- 20 (5) In discharging his or her administrative duties under this section, a trustee shall
- 21 strive to administer the retirement system in an efficient and cost-effective manner
- 22 for the taxpayers of the Commonwealth of Kentucky.
- 23 (6) Notwithstanding any other provision of KRS 161.220 to 161.716, no funds of the
- 24 Teachers' Retirement System, including fees and commissions paid to an
- 25 investment manager, private fund, or company issuing securities, who manages
- 26 systems assets, shall be used to pay fees and commissions to placement agents. For
- 27 purposes of this subsection, "placement agent" means a third-party individual, who

1 is not an employee, or firm, wholly or partially owned by the entity being hired,
2 who solicits investments on behalf of an investment manager, private fund, or
3 company issuing securities.

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

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

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

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

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

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

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

- 1 (8) (a) The board shall adopt written proxy voting guidelines which are consistent
2 with the fiduciary duties and other requirements of this section.
- 3 (b) The board shall not adopt the recommendations of a proxy adviser or proxy
4 voting service and shall not allow such proxy adviser or proxy voting service
5 to vote on behalf of the system, unless the proxy adviser or proxy voting
6 service acknowledges in writing and accepts under contract its duties under
7 this section and commits to follow the board-adopted proxy voting guidelines
8 when voting the system's shares in order to comply with the board's fiduciary
9 duties and other responsibilities under this section.
- 10 (c) All shares held by or on behalf of the system, and which the system is entitled
11 to vote under state, federal, or common laws, shall be voted according to the
12 proxy voting guidelines adopted by the board and subject to the fiduciary
13 duties and other requirements of this section by:
- 14 1. The board, the investment committee of the board, or an employee or
15 employees of the system who are fiduciaries under this section and are
16 appointed or otherwise authorized by the board; or
- 17 2. A proxy adviser or proxy voting service that acknowledges in writing
18 and accepts under contract its duties under this section and commits to
19 follow the board-adopted proxy voting guidelines when voting the
20 system's shares in order to comply with the board's fiduciary duties and
21 other responsibilities under this section.
- 22 (d) All proxy votes shall be reported at least quarterly to the board. For each vote,
23 the report shall provide:
- 24 1. The vote caption;
25 2. The date of the vote;
26 3. The company's name;
27 4. The vote cast for the system;

- 1 5. The recommendation of the company's management; and
- 2 6. If applicable, the recommendation of the proxy adviser or proxy voting
- 3 service.