



Kentucky Retirement Systems

Statement of Investment Policy-Insurance Fund

This statement of investment policy is issued by the Board of Trustees of Kentucky Retirement Systems in connection with investing the funds of the Kentucky Retirement Systems Insurance Fund. This document supersedes all prior documents entitled Statement of Investment Policy.

I. The Board of Trustees

The Kentucky Retirement Systems is a "Qualified Pension Plan" under Section 401 of the Internal Revenue Code and is administered by a board of nine trustees. Three trustees are appointed by the Governor of the Commonwealth of Kentucky, two trustees are elected by the membership of the Kentucky Employees Retirement System, two trustees are elected by the membership of the County Employees Retirement System, and one trustee is elected by the membership of the State Police Retirement System. The Secretary of the Personnel Cabinet is an ex-officio trustee.

KRS 61.701 establishes the "Kentucky Retirement Systems Insurance Fund" as a separate fund to provide fringe benefits to recipients of the Kentucky Employees Retirement System, County Employees Retirement System and State Police Retirement System. KRS 61.702 provides that all amounts necessary to provide for insurance benefits shall be paid to the insurance fund. The Board shall administer the fund in the same manner as the retirement funds.

The Board of Trustees authorizes and directs the appointment of an Investment Committee with full power to act for the board in the acquisition, sale and management of the securities and funds of the Systems in accordance with the provisions of the Statutes and Investment Policy of the Board. The Board shall review the actions of the Investment Committee at each quarterly Board meeting.

II. The Investment Committee

The Investment Committee consists of five members of the Board of Trustees appointed by the chairperson of the Board of Trustees. The committee acts on behalf of the board on investment related matters.

The Investment Committee has the following oversight responsibilities:

- A. Assure compliance with this policy and all applicable laws and regulations.
- B. Approve the selection and termination of service providers.
- C. Meet quarterly to evaluate whether this policy, the investment activities and management controls and processes continue to be consistent with meeting the Systems' goals. Mandate actions necessary to maintain the overall effectiveness of the program.
- D. Review assessment of investment program management processes and procedures, and this policy relative to meeting stated goals.

III. Staff Responsibilities

The Chief Investment Officer is responsible for administration of investment assets of the Systems consistent with the policies, guidelines and limits established by the law, this Statement of Investment Policy and the Investment Committee.

The Chief Investment Officer receives direction from and reports to the Investment Committee and the Executive Director of the Systems on all investment matters, including but not limited to the following:

- A. Maintaining the diversification and risk exposure of the funds consistent with policies and guidelines.
- B. Monitoring and assessing service providers, including annual on site visits, to assure that they meet expectations and conform to policies and guidelines.
- C. Assess and report on the performance and risk exposure of the overall investment program relative to goals, objectives, policies and guidelines.
- D. Recommend changes to service providers, statutes, policies or guidelines as needed to maintain a productive relationship between the investment program and its goals; act as liaison on all investment related matters.
- E. Communicating with the mass media and other agencies, entities or institutions regarding investment related issues.
- F. Identify issues for consideration by the Investment Committee and prepare recommendations regarding such matters.

The Chief Investment Officer or designee is authorized to execute trades on fixed income and equities and to execute proxies for the Board consistent with this Policy.

To carry out this Policy and investment related decisions of the Board, the Chief Investment Officer or designee is authorized to execute agreements and other necessary or proper documents pertaining to investment managers, consultants, investment related transactions or other investment functions.

IV. Service Providers

A. Investment Managers

In instances where the Investment Committee has determined it is desirable to employ the services of an external Investment Manager, the following shall be applicable:

1. Investment Managers shall be qualified to serve as fiduciaries to the Systems and shall have been in the business of investment management for large United States pension fund assets at least five years.
2. Investment Managers shall manage assets in accordance with this Policy and additional guidelines established by contract, as may be modified from time to time.

B. Custody Bank

The Board shall hire custodians and other agents who will be fiduciaries to the Systems and who will assume responsibility for the safekeeping and accounting of all assets held on behalf of the Systems and other duties as agreed to by contract.

C. Investment Consultants

Qualified independent investment consultants may be retained by the Systems for asset allocation studies, asset allocation recommendations, performance reviews, manager searches and other investment related consulting functions and duties as set forth by contract.

D. Selection

Qualified investment managers, custody banks, investment consultants and other service providers shall be selected by the Investment Committee or Chief Investment Officer as required. The selection shall be based upon the demonstrated ability of the professional(s) to provide the required expertise or assistance. In order to create an efficient and effective process, the Investment Committee or Chief Investment Officer may, in their sole discretion, utilize RFI, RFP, third party proprietary software or database, review of existing service provider capabilities or any combination of these or other methods to select a service provider. Relevant criteria for the selection of investment managers are contained in the Transactions Procedures statement.

All contact and communication with service providers seeking a business relationship with the Systems shall be directed to the Chief Investment Officer. However, this rule is not applicable to existing service providers if the contact or communication is in response to an information request from the Investment Committee or if it is incidental contact not related to specific Systems business.

V. Investment Philosophy

The Trustees of the Kentucky Retirement Systems recognize their fiduciary duty not only to invest the Systems' funds in formal compliance with the Prudent Person Rule but also to manage those funds in continued recognition of the basic long term nature of those systems. The Trustees interpret this to mean, in addition to the specific guidelines and restrictions set forth in this document that the assets of the fund shall be actively managed -- that is, investment decisions regarding the particular securities to be purchased or sold shall be the result of the conscious exercise of discretion.

The Trustees recognize that, commensurate with their overall objective of maximizing long-range return while maintaining a high standard of portfolio quality and consistency of return, it is necessary that proper diversification of assets be maintained both among and within the classes of securities held. Consistent with carrying out their Fiduciary Responsibilities and the concept of Modern Portfolio Theory, the Trustees will not systematically exclude any investments in companies, industries, countries, or geographic areas. Within this context of active management and the necessity for adherence to proper diversification, the Trustees rely upon appropriate professional advice.

The Trustees and other fiduciaries shall discharge their duties with respect to the Systems: (1) solely in the interest of the participants and beneficiaries; (2) for the exclusive purpose of providing benefits to participants and beneficiaries; (3) with the care, skill and caution under the circumstances then prevailing which 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; (4) impartially; (5) incurring and paying appropriate and reasonable expenses of administration and (6) in accordance with a good faith interpretation of the laws, regulations and other instruments governing the Systems.

Additionally, the Trustees and other fiduciaries shall not engage in any transaction which results in a substantial diversion of the Systems income or assets without adequate security and reasonable rate of return to a disqualified person or in any other prohibited transaction described in Internal Revenue Code Section 503(b).

VI. Investment Objectives

The Board of Trustees realizes that prudent investment management is a duty. In fulfillment of this duty the Board of Trustees recognizes that while long-term objectives are important, it is also necessary that short-term benchmarks be used to assess the periodic performance of the investment program.

Accordingly, the Board of Trustees has established the following investment objectives for the insurance fund:

- Long-Term:
 - The total assets of the Systems should achieve a return measured over two market cycles (estimated to be six to ten years) which exceeds the actuarially required rate of return of 7.75%, which consists of two components; an inflation component and a real return component. The current assumption for the rate of inflation is 3.5% and the real return component is 4.25%.
 - In addition to the actuarially required rate of return benchmark, the total fund return should exceed the return achieved by its blended performance benchmark.
- Short-Term:
 - The returns of the particular asset classes of the managed funds of the Systems, measured on a year-to-year basis, should exceed the returns achieved by comparable unmanaged market indices as described in the section of this statement entitled "Standards of Measurement."

VII. Derivative Securities and Leveraging

Derivative Securities

Investment managers may invest in derivative securities, or strategies which make use of derivative investments, only if such investments do not cause the portfolio to be in any way leveraged beyond a 100% invested position. Examples of such derivatives include, but are not limited to, foreign currency forward contracts, collateralized mortgage obligations (CMOs), treasury inflation protected securities (TIPS), futures, options, and swaps.

Investments in derivative securities which are subject to large or unanticipated changes in duration or cash flows, such as interest only (IO), principal only (PO), inverse floater, or structured note securities are permitted only to the extent authorized in an alternative investment offering memorandum or agreement.

Investments in securities such as collateralized mortgage obligation (CMO) and planned amortization class (PAC) issues are allowed if, in the judgment of the investment manager, they are not expected to be subject to large or unanticipated changes in duration or cash flows. Investment managers may make use of derivative securities for defensive or hedging purposes.

Any derivative security shall be sufficiently liquid that it can be expected to be sold at, or near, its most recently quoted market price.

Leveraging

Leveraging for purposes of enhancing yield is expressly prohibited except for investments in the alternative asset class. Managers of alternative investments are granted the authority to engage in positive leverage to the extent authorized in their offering memorandum or agreement.

The above is not intended to limit the Systems from borrowing to cover short-term cash flow needs nor prohibit the Systems from loaning securities in accordance with a securities lending agreement.

VIII. Asset Allocation Guidelines

In establishing asset allocation guidelines the Board recognizes that the insurance fund has its own capacity to tolerate investment volatility, or risk. Starting with fiscal year 1994-95 the Board will cause the asset allocation guidelines of each system to be studied again. Subsequent to that study, the Board will cause additional studies of the asset allocation guidelines to be performed at approximate five year intervals in conjunction with the Systems Actuarial Experience Study.

The intent of the Board of Trustees in allocating funds to the investment managers is for the investment managers to fully invest the funds. However, the Board of Trustees is aware that from time to time the investment managers will require a portion of the allocated funds to be held in cash provided the cash holdings do not exceed three percent (3%) of the manager's allocation for any given quarter, unless such cash holdings are an integral part of a fixed income manager's investment strategy.

Based on market value, the following are the allowable ranges for the fund:

Asset Class	Target	Allowable Range
Domestic Equity	40.0%	30-70%
International Equity	30.0%	20-40%
Fixed Income – TIPS*	10.0%	0-15%
Fixed Income- Market*	0.0%	0-30%
Alternative Investments	15.0%	1-20%
Cash Equivalents*	3.0%	1-10%

* At no time will the fund's assets have less than 10% of the total allocated to the combination of fixed income and cash equivalents.

The actual asset class allocation of the Insurance Fund will be reviewed monthly by staff relative to its target asset class allocation. Staff shall reallocate the assets when the actual asset class allocation is within one percentage point of the allowable range boundary, but may reallocate when the actual asset class allocation exceeds the target asset class allocation by a margin of +/- 1 percentage points.

In keeping with its responsibility as trustee and wherever consistent with its fiduciary responsibility, the

board encourages the investment of the fund's assets in securities of corporations which provide a positive contribution to the economy of the Commonwealth of Kentucky. However, where any security is not a prohibited investment under the governing laws and policies, discretion will be granted to the appointed investment managers in the selection of such securities and timing of transactions consistent with the following guidelines and restrictions.

A. Domestic Equity Investments

Investment may be made in common stock of publicly traded companies on stock markets or any other type of security contained in a manager's benchmark. Each individual domestic equity account shall have a comprehensive set of investment guidelines prepared, which contains a listing of permissible investments, portfolio restrictions and standards of performance for the account.

The internally managed equity index funds are intended, consistent with the governing plan documents, to gain exposure to a broad asset sector to replicate the characteristics of the asset class, to minimize administrative expenses and to help achieve overall portfolio objectives. These objectives can be achieved through several management techniques, including but not limited to, portfolio optimization, non-reinvestment of index dividends and other management techniques intended to help achieve the objectives of the entire insurance fund.

B. International Equity Investments

Investment may be made in common stock, securities convertible into common stock and in preferred stock of publicly traded companies on stock markets, or any other type of security contained in a manager's benchmark. Each individual international equity account shall have a comprehensive set of investment guidelines prepared, which contains a listing of permissible investments, portfolio restrictions and standards of performance for the account.

The internally managed equity index funds are intended, consistent with the governing plan documents, to gain exposure to a broad asset sector to replicate the characteristics of the asset class, to minimize administrative expenses and to help achieve overall portfolio objectives. These objectives can be achieved through several management techniques, including but not limited to, portfolio optimization, non-reinvestment of index dividends and other management techniques intended to help achieve the objectives of the entire insurance fund.

C. Fixed Income Investments

Investment may be made in the various classes of fixed income instruments as follows:

- Corporate Bonds. Publicly traded bonds are to be selected and managed so as to assure an appropriate balance in quality and maturities consistent with current market and economic conditions. Although active bond management is encouraged, excessive emphasis on short-term trading is not considered appropriate. Private or direct placement bonds may be purchased only upon specific approval by the Investment Committee of the Board of Trustees.
- Government & Agency Bonds. Investment may be made in notes, other interest-bearing obligations and purchases of participation in such instruments that are issued or guaranteed in whole or in part by the United States of America or by any agency or instrumentality thereof.
- Mortgages. Investments may be made in real estate mortgages on a direct issue basis or in

the form of mortgage pool instruments guaranteed by an agency of the U.S. Government or by the Commonwealth of Kentucky.

- High Yield Bonds. Investments may be made in bonds that have ratings of BBB or Baa or lower according to the standard rating agencies.

Each individual fixed income account shall have a comprehensive set of investment guidelines prepared, which contains a listing of permissible investments, portfolio restrictions and standards of performance for the account.

D. Alternative Investments

Subject to specific approval of the Investment Committee of the Board of Trustees, investments may be made for the purpose of creating a diversified portfolio of alternative investments. Examples of such investments include, but are not limited to, venture capital partnerships, private equity, leveraged buyouts and funds, private debt, timberland, oil and gas partnerships, commodities and private placements. While it is expected that the majority of these assets will be invested within the United States, a portion has been allocated to non-US investments, with a primary focus on Europe.

It is expected that these investments will typically be structured as Limited Partnerships, with KRS serving as one of the Limited Partners, but not as a General Partner. It is also expected that KRS will not engage in direct investments or co-investments, in which the System would purchase majority control in individual corporate entities.

Funds that are committed to said Limited Partnerships, but not yet drawn down by the General Partner, will be invested in the Systems' internally managed equity funds, as the risk/reward characteristics of these funds most closely match those of the Limited Partnerships.

The following sub-asset allocations, based on invested value, are to be consistent with the overall asset allocation of the Total Insurance Fund, as well as the investable universe within private equity. The ranges reflect long-term averages, once the 5% allocation to Alternatives has been fully committed. During the initial investment period, approximately four to six years, it is expected that sub-category allocations may fall outside the approved ranges.

<u>Sub-Category</u>	<u>Target Allocations</u>	<u>Ranges</u>
Venture Capital	20.0%	10-30%
Buyouts	50.0%	40-60%
Debt-Related	10.0%	0-20%
International	20.0%	0-30%

E. Real Estate Investments

Subject to specific approval of the Investment Committee of the Board of Trustees, Investments may be made in equity and debt real estate for the purpose of achieving the highest total rate of return possible consistent with a prudent level of risk. Allowable real estate investments include open-end and closed-end commingled real estate funds, joint venture investments, public and

private REITs (real estate investment trusts), public real estate operating companies, and real estate related debt . The target allocation for this asset class is 5% of the aggregate portfolio.

Real estate investments will be allocated across the core, enhanced/value added, and opportunistic categories.

F. Cash Equivalent Securities

Selection of particular short-term instruments, whether viewed as liquidity reserves or as alternative investment vehicles, should be determined primarily by the safety and liquidity of the investment and only secondarily by the available yield. The following short-term investment vehicles are considered acceptable:

Publicly traded investment grade corporate bonds, government and agency bonds, mortgages, and collective STIFs, money market funds or instruments (including, but not limited to, certificates of deposit, bank notes, deposit notes, bankers' acceptances and commercial paper) and repurchase agreements relating to the above instruments. Instruments may be selected from among those having an investment grade rating at the time of purchase by at least one recognized bond rating service. In cases where the instrument has a split rating, the higher of the two ratings shall prevail.

All instruments shall have a maturity at the time of purchase that does not exceed two years. Repurchase agreements shall be deemed to have a maturity equal to the period remaining until the date on which the repurchase of the underlying securities is scheduled to occur.

The Systems' fixed income managers that utilize cash equivalent securities as an integral part of their investment strategy are exempt from the permissible investments contained in the preceding paragraph. Permissible short-term investments for fixed income managers shall be included in the investment manager's investment guidelines.

IX. Standards of Measurement

The following represent the standards of measurement to be used as guidelines for the various classes of investments of the Kentucky Retirement Systems Insurance Fund. They are to be computed and expressed on a time-weighted return basis:

A. Domestic Equity Allocation

Total Domestic Equity Allocation: The Total Domestic Equity Allocation shall be benchmarked to the Russell 3000 Index and comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, the Total Domestic Equity Allocation should exceed the returns of the Russell 3000 Index.
- Intermediate & Long-term
 - For periods greater than five years or one market cycle, the Total Domestic Equity Allocation should exceed the Russell 3000 Index, compare favorably on a risk-adjusted basis, and generate returns that rank above the median return of a relevant

peer group. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the Index.

Individual Equity Portfolios: Individual portfolios shall be assigned a market goal or benchmark that is representative of the style or market capitalization of the assignment. Individual equity accounts should comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, individual portfolios should exceed the returns of their market goal or benchmark.
- Intermediate & Long-term
 - For periods greater than five years or one market cycle, individual portfolios should exceed the return of their market goal or benchmark, compare favorably on a risk-adjusted basis, and generate returns that rank above the median return of a relevant peer group. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the benchmark.

B. International Equity Allocation

Total International Equity Allocation: The Total International Equity Allocation shall be benchmarked to the MSCI All Country World ex-US Index and comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, the Total International Equity Allocation should exceed the returns of the MSCI All Country World ex-US Index.
- Intermediate & Long-term
 - For periods greater than five years or one market cycle, the Total International Equity Allocation should exceed the MSCI All Country World ex-US Index, compare favorably on a risk-adjusted basis, and generate returns that rank above the median return of a relevant peer group. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the Index.

Individual International Equity Portfolios: Individual portfolios shall be assigned a market goal or benchmark that is representative of the style or market capitalization of the assignment. Individual equity accounts should comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, individual portfolios should exceed the returns of their market goal or benchmark.
- Intermediate & Long-term
 - For periods greater than five years or one market cycle, individual portfolios should exceed the return of their market goal or benchmark, compare favorably on a risk-adjusted basis, and generate returns that rank above the median return of a relevant peer group. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the benchmark.

C. Fixed Income Allocation

Total Fixed Income Allocation: The Total Fixed Income Allocation shall be benchmarked to a KRS High Yield Index and comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, the Total Fixed Income Allocation should exceed the returns of the KRS High Yield Index.
- Intermediate & Long-term
 - For periods greater than five years or one market cycle, the Total Fixed Income Allocation should exceed the KRS High Yield Index, compare favorably on a risk-adjusted basis, and generate returns that rank above the median return of a relevant peer group. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the Index.

Individual Fixed Income Portfolios: Individual portfolios shall be assigned a market goal or benchmark that is representative of the style or market capitalization of the assignment. Individual portfolios should comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, individual portfolio accounts should exceed the returns of their market goal or benchmark.
- Intermediate & Long-term
 - For periods greater than five years or one market cycle, individual portfolios should exceed the return of their market goal or benchmark, compare favorably on a risk-adjusted basis, and generate returns that rank above the median return of a relevant peer group. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the benchmark.

D. Fixed Income – TIPS

Total TIPS Allocation: The Total TIPS Allocation shall be benchmarked to the Lehman Brothers TIPS Index and comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, the Total TIPS Allocation should exceed the returns of the Lehman Brothers TIPS Index.
- Intermediate & Long-term
 - For periods greater than five years or one market cycle, the Total TIPS Allocation should exceed the Lehman Brothers TIPS Index and compare favorably on a risk-adjusted basis. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the Index.

Individual TIPS Portfolios: Individual portfolios shall be assigned a market goal or benchmark that is representative of the style or market capitalization of the assignment. Individual portfolios should comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, individual portfolio accounts should exceed the returns of their market goal or benchmark.
- Intermediate & Long-term

- For periods greater than five years or one market cycle, individual portfolios should exceed the return of their market goal or benchmark and compare favorably on a risk-adjusted basis. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the benchmark.

E. Alternative Investments

Total Alternative Investment Allocation: The Total Alternative Investment Allocation shall have a performance benchmark that consists of the Russell 3000 Index plus 300 basis points. Alternative Investment sub-class segments shall be assigned a performance benchmark and comply with relevant Standards.

Venture Capital

Description: Venture capital investments are seed stage, early stage, later stage, and expansion stage investments. Investments are often made in years one through five and distributions typically occur in years four through ten.

Investment Constraints: No more than 35% of total net assets of an individual partnership may be invested in securities or obligations of foreign entities issued outside the U.S. No more than 50% of total net assets of an individual partnership may be invested in a single segment within a particular industry.

Performance Standards:

- Short-term
 - For periods less than five years, Venture Capital investments should earn a Net IRR that place the investment above the median Net IRR of other similar venture capital funds, of the same vintage year, as reported by Venture Economics.
- Intermediate & Long-term
 - For periods greater than five years, Venture Capital investments should earn a Net IRR that exceeds the Russell 3000 Index plus 500 basis points (annualized) and that place the investment above the median Net IRR of other similar venture capital funds, of the same vintage year, as reported by Venture Economics.

Buyouts

Description: Buyout investments typically involve the purchase of a control position (primarily majority positions, with some minority positions) in an established company. Leverage may be used. Investments are often made in years one through four and distributions typically occur in years three through six.

Investment Constraints: No more than 35% of total net assets of an individual partnership may be invested in securities or obligations of foreign entities issued outside the U.S. No more than 50% of total net assets of an individual partnership may be invested in a single segment within a particular industry.

Performance Standards:

- Short-term
 - For periods less than five years, Buyout investments should earn a Net IRR that place the investment above the median Net IRR of other similar buyout funds, of the same vintage year, as reported by Venture Economics.
- Intermediate & Long-term
 - For periods greater than five years, Buyout investments should earn a Net IRR that exceeds the Russell 3000 Index plus 300 basis points (annualized) and that place the investment above the median Net IRR of other similar buyout funds, of the same vintage year, as reported by Venture Economics.

Debt-Related

Description: Debt-related investments combine a debt instrument, which provides a current yield, with an equity participation in warrants, etc. Investments are typically made in years one through three and provide current income combined with capital appreciation supplied by the warrants or other “equity kickers”.

Investment Constraints: No more than 35% of total net assets of an individual partnership may be invested in securities or obligations of foreign entities issued outside the U.S. Investments may be made in equity or debt related real estate assets. The General Partner may not purchase securities on margin or otherwise borrow funds for the purposes of purchasing securities.

Performance Standards:

- Short-term
 - For periods less than five years, Debt-related investments should earn a Net IRR that place the investment above the median Net IRR of other similar debt-related funds, of the same vintage year, as reported by Venture Economics.
- Intermediate & Long-term
 - For periods greater than five years, Debt-related investments should earn a Net IRR that exceeds the Russell 3000 Index plus 300 basis points (annualized) and that place the investment above the median Net IRR of other similar debt-related funds, of the same vintage year, as reported by Venture Economics.

International

There are no separate guidelines for international investments. Specific guidelines for these investments are included within the sections covering buyout, venture capital, and debt related investments. To ensure prudent diversification and due to the unique characteristics of international private equity markets, it is expected that international exposure will be provided by one or more fund-of-fund vehicles, rather than through direct partnership investments.

F. Real Estate

REITS

Description: A portfolio which invests in a pool of publicly traded real estate securities, providing capital appreciation, inflation protection, and current income.

Investment Constraints: The strategy must invest in real estate securities trade on public exchanges in the United State, Europe, or Asia.

Benchmark: EPRA/NAREIT Global Real Estate Index

Core Private Real Estate

Description: Direct private investment in equity and debt real estate funds, private REITs, joint ventures, and partnerships. Core real estate funds typically provide more current income than Value-Added/Oppportunistic real estate but less potential for capital appreciation. Core also typically uses less leverage (debt financing) than Value-Added/Oppportunistic real estate.

Investment Constraints: No more than 50% leverage may be used at the portfolio level.

Benchmark: NCREIF Index.

Value-Added/Oppportunistic Private Real Estate

Description: Direct private investment in equity and debt real estate funds, private REITs, joint ventures, and partnerships. Opportunistic and enhanced/value-added funds typically provide less current income than core real estate, and use more leverage (debt financing) than core real estate.

Investment Constraints: No more than 80% leverage for a value-added fund.

Benchmark: NCREIF plus 200 basis points for value-added funds and NCREIF plus 500 basis points for opportunistic funds.

G. Cash Equivalents Allocation

Total Cash Equivalents Allocation: The Total Cash Equivalents Allocation shall be benchmarked to the Citigroup 3-month Treasury Bill Index and comply with the following Standards:

- Short-term
 - For periods less than five years or a full market cycle, the Total Cash Equivalents Allocation should exceed the returns of the Citigroup 3-month Treasury Bill Index.
- Intermediate & Long-term
 - For periods greater than five years or one market cycle, the Total Cash Equivalents Allocation should exceed the Citigroup 3-month Treasury Bill Index and compare favorably on a risk-adjusted basis. Volatility, as measured by the standard deviation of monthly returns, should be comparable to the Index.

X. Investments Performance Review Procedures

On a timely basis, but not less than quarterly, the Investment Committee, on behalf of the Board of Trustees, will review the performance of the fund for determination of compliance with this Statement of Investment Policy. On an annual basis, a comprehensive review of each asset class and underlying portfolios shall be conducted by the staff and presented to the Investment Committee. The review shall consist of an organizational, performance and compliance assessment.

The Chief Investment Officer or designee shall perform tests each month to assure compliance with the restrictions imposed by this policy. These tests shall be performed at the asset class and total fund level. Investment managers shall notify the Kentucky Retirement Systems immediately upon detection of non-compliance with any of the following restrictions. These restrictions are not applicable to those funds invested in indexed equities or Alternative Investments. Quarterly, the Chief Investment Officer or designee shall prepare a report to the Investment Committee detailing the restrictions tested, exceptions, the cause of the exception and the subsequent resolution. The Investment Committee shall report the findings to the Board of Trustees at the next regularly scheduled meeting.

The following restrictions shall be tested monthly:

- ▶ The amount of stock in the domestic or international equity allocation in any single corporation shall not exceed 5% of the aggregate market value of the Systems' assets.
- ▶ The amount of stock held in the domestic or international equity allocation shall not exceed 3% of the outstanding shares of any single corporation.
- ▶ The amount of stock in any one industry in the domestic equity allocation shall not exceed 10% of the aggregate market value of the System's assets.
- ▶ The amount invested in emerging markets shall not exceed 30% of the Systems' international equity assets. Investments in emerging markets shall be made primarily in countries included in the MSCI Emerging Markets Index. Investment in "frontier" markets (those countries not included in the MSCI EM Index) shall not exceed 10% of the System's international equity assets.
- ▶ The duration of the total fixed income portfolio shall not deviate from the KRS High Yield Index by more than 10%.
- ▶ The duration of the TIPS portfolio shall not deviate from the Lehman Brothers TIPS Index by more than 10%.
- ▶ No public fixed income manager shall invest more than 5% of the market value of assets held in any single issue short term instrument, with the exception of U.S. Government issued, guaranteed or agency obligations.

The Chief Investment Officer shall develop a comprehensive set of investment guidelines for each externally managed account. These guidelines should ensure, at the total fund and asset class level, that the restrictions set forth above are preserved. The Chief Investment Officer or designee shall perform tests each month to assure compliance with the guidelines. Quarterly, the Chief Investment Officer or designee shall prepare a report to the Investment Committee detailing the restrictions tested, exceptions, the cause of the exception and the subsequent resolution. The Investment Committee shall report the findings to the Board of Trustees at the next regularly scheduled meeting

XI. Additional Items

A. Proxy Voting

The Board of Trustees reserves the right to direct the Chief Investment Officer, or designee, to vote proxies in accordance with the Investment Committee Proxy Voting Policy, which is hereby incorporated by reference.

B. Brokerage Policy

The Investment Committee brokerage policy is hereby incorporated by reference.

C. Transaction Procedures

The Investment Committee transaction procedures are hereby incorporated by reference.

D. Securities Litigation Policy and Procedures

The Investment Committee securities litigation policy and procedures are hereby incorporated by reference.

E. Securities Lending Guidelines

The Investment Committee securities lending policy and procedures are hereby incorporated by reference.

F. Securities Trading Policy for Trustees and Employees

The Kentucky Retirement Systems trading policy for Trustees and employees is hereby incorporated by reference.

As Adopted By
The Board of Trustees
Kentucky Retirement Systems

Date: November 15, 2007

Chair
Board of Trustees