Financial Section

for Fiscal Year ending June 30, 2013

Mountjoy
Chilton
Medley

Independent Auditor's Report on Financial Statements

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

Report on the Financial Statements

We have audited the accompanying statements of the plan net position of the Teachers' Retirement System of the State of Kentucky as of and for the years ended June 30, 2013 and 2012, and the related statements of changes in plan net position for the years then ended, and the related notes to the financial statements which collectively comprise the component unit financial statements of the Teachers' Retirement System of the State of Kentucky as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective plan net position of the Teachers' Retirement System of the State of Kentucky, a component unit of the Commonwealth of Kentucky, as of June 30, 2013 and 2012, and the respective changes in its plan net position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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Independent Auditor's Report on Financial Statements

Other Matters

Required Supplementary Information
Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 18 through 21 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 16, 2013, on our consideration of the Teachers' Retirement System of the State of Kentucky's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Teachers' Retirement System of the State of Kentucky's internal control over financial reporting and compliance.

Mountjoy Chilton Medley LLP

Mountjoy Chilton Medley LLP

Lexington, KY
December 16, 2013

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

This discussion and analysis of The Teachers' Retirement System of the State of Kentucky (Kentucky Teachers' Retirement System, KTRS, System, or Plan) financial performance provides an overview of the defined benefit and medical insurance plans' financial year ended June 30, 2013. Please read it in conjunction with the respective financial statements, which begin on page 22.

USING THIS FINANCIAL REPORT

Because of the long-term nature of the defined benefit retirement annuity plan, and the medical and life insurance plans, financial statements alone cannot provide sufficient information to properly reflect the ongoing perspective of the System. The Statement of Plan Net Position and Statement of Changes in Plan Net Position (on pages 22-25) provide information about the activities of the defined benefit retirement annuity plan, medical insurance plan, life insurance plan and the tax-sheltered annuity plan as a whole. The Kentucky Teachers' Retirement System is the fiduciary of funds held in trust for its members.
The Schedule of Funding Progress (on pages 50 and 51) includes historical trend information about the actuarially funded status of each plan from a long-term, ongoing plan perspective and the progress made in accumulating sufficient assets to pay benefits and insurance premiums when due. The Schedule of Employer Contributions (on pages 50 and 51) presents historical trend information about the annual required contributions of employers and the contributions made by employers in relation to the requirement. These schedules provide information that contributes to understanding the changes over time in the funded status of the plans.

KENTUCKY TEACHERS' RETIREMENT SYSTEM AS A WHOLE

In the fiscal year ended June 30, 2013, Kentucky Teachers' Retirement System's combined plan net position increased by $1,384.3 million - from $15,229.1 million in 2012 to $16,613.4 million in 2013. In 2011, the combined net position totaled $15,514.9 million. The following summaries focus on plan net position and changes in plan net position of Kentucky Teachers' Retirement System's defined benefit retirement annuity plan, medical insurance plan, life insurance plan and other funds.

Summary of Plan Net Position
(In Millions)

Categories	Defined Benefit Plan			Medical Insurance Plan			Life Insurance Fund		
	2013	2012	2011	2013	2012	2011	2013	2012	2011
Cash & Investments	$ 16,549.7	$ 15,123.6	$ 15,192.9	$ 456.5	$ 345.0	$ 429.2	$ 88.8	$ 91.1	$ 87.4
Receivables	173.0	133.4	180.7	16.8	16.3	5.3	1.1	1.1	1.1
Capital Assets	9.2	6.8	3.8	.	.	.			
Total Assets	16,731.9	15,263.8	15,377.4	473.3	361.3	434.5	89.9	92.2	88.5
Total Liabilities	(623.1)	(466.7)	(246.8)	(59.6)	(22.5)	(139.7)			
Plan Net Position	$ 16,108.8	$ 14,797.1	$ 15,130.6	$ 413.7	$ 338.8	$ 294.8	$ 89.9	$ 92.2	$ 88.5

*TOTALS	2013	2012	2011
Cash & Investments	$ 17,095.0	$ 15,559.7	$ 15,709.5
Receivables	190.9	150.8	187.1
Capital Assets	9.2	6.8	3.8
Total Assets	17,295.1	15,717.3	15,900.4
Total Liabilities	(682.7)	(489.2)	(386.5)
Plan Net Assets	$ 16,612.4	$ 15,228.1	$ 15,513.9

* *Other Funds consisting of the 403(b) Tax Shelter Plan, the Excess Benefit Fund and the Losey Scholarship fund had a combined plan net position of $.9 million for years ended 2013, 2012 and 2011.*

The plan net position of the defined benefit retirement annuity plan increased by 8.9 percent ($16,108.8 million compared to $14,797.1 million) and in 2011, the plan net position of the defined benefit plan totaled $15,130.6 million. The increase is primarily due to improvements in market conditions which resulted in a net investment income increase of $1.73 billion more than 2012. The 2013 amount was $.72 billion less than 2011. The defined benefit retirement annuity plan assets are restricted to providing monthly retirement allowances to members and their beneficiaries. Plan net position of the medical insurance plan increased by 22.1 percent ($413.7 million compared to $338.8 million) primarily due to contributions from members and employers exceeding insurance expenses due to legislation passed in 2010. This compares to 2011 where plan net position of the medical insurance fund totaled $294.8 million. Plan assets are restricted to providing hospital and medical insurance benefits to members and their spouses.

Summary of Changes in Plan Net Position

(In Millions)

Categories	Defined Benefit Plan 2013	2012	2011	Medical Insurance Plan 2013	2012	2011	Life Insurance Fund 2013	2012	2011
ADDITIONS									
Member Contributions	$ 304.7	$ 309.8	$ 302.3	$ 119.8	$ 100.3	$ 84.1	$	$	$
Employer Contributions	568.2	557.3	1,037.9	166.6	174.0	188.3	1.7	1.7	1.7
Net Investment Income	2,039.9	309.7	2,761.0	30.7	(4.0)	8.3	0.7	6.4	3.1
Other Income					3.8	0.5			
TOTAL ADDITIONS	2,912.8	1,176.8	4,101.2	317.1	274.1	281.2	2.4	8.1	4.8
DEDUCTIONS									
Benefit Payments	1,570.7	1,482.9	1,402.6				4.6	4.4	4.2
Refunds	22.1	19.5	17.3						
Administrative Expense	8.4	7.8	7.3	1.3	1.2	1.2			
Insurance Expenses				240.9	229.0	226.4			
TOTAL DEDUCTIONS	1,601.2	1,510.2	1,427.2	242.2	230.2	227.6	4.6	4.4	4.2
Increase (Decrease) in Plan Net Position	$ 1,311.6	$ (333.4)	$ 2,674.0	$ 74.9	$ 43.9	$ 53.6	$ (2.2)	$ 3.7	$ 0.6

TOTALS	2013	2012	2011
ADDITIONS			
Member Contributions	$ 424.5	$ 410.1	$ 386.4
Employer Contributions	736.5	733.0	1,227.9
Net Investment Income	2,071.3	312.1	2,772.4
Other Income		3.8	0.5
TOTAL ADDITIONS	3,232.3	1,459.0	4,387.2
DEDUCTIONS			
Benefit Payments	1,575.3	1,487.3	1,406.8
Refunds	22.1	19.5	17.3
Administrative Expense	9.7	9.0	8.5
Insurance Expenses	240.9	229.0	226.4
TOTAL DEDUCTIONS	1,848.0	1,744.8	1,659.0
Increase (Decrease) in Plan Net Assets	$ 1,384.3	$ (285.8)	$ 2,728.2

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

DEFINED BENEFIT RETIREMENT ANNUITY PLAN ACTIVITIES

Member contributions decreased $5.1 million. Retirement contributions are calculated by applying a percentage factor to salary and are paid monthly by each member. Members may also pay contributions to repurchase previously refunded service credit or to purchase various types of elective service credit.

Employer contributions totaled $568.2 million, a net increase of $10.9 million from the 2012 fiscal year.

The System experienced an increase in net investment income compared to the previous year ($2,039.9 million at June 30, 2013 as compared to a $309.7 million at June 30, 2012). For 2011, net investment income totaled $2,761.0 million. The increase in the fair value of investments is mainly due to favorable market conditions for the year ended June 30, 2013 and is illustrated as follows:

Dollar Amount in Millions

	2013	2012	2011
Appreciation (depreciation) in fair value of investments – June 30, prior year	$ 1,411.6	$ 1,842.0	$ (235.5)
Appreciation (depreciation) in fair value of investments – June 30, end of year	2,428.5	1,411.6	1,842.0
Change in net appreciation (depreciation) in fair value of investments	1,016.9	(430.4)	2,077.5
Net income (net of investment expense)	438.1	378.2	362.3
Net gain on sale of investments	548.9	361.9	321.2
Investment Income (net) – June 30, end of year	$ 2,039.9	$ 309.7	$ 2,761.0

Program deductions in 2013 increased $91.0 million. The increase was caused principally by an increase of $87.8 million in benefit payments. Members who were drawing benefits as of June 2012 received an increase of one and one-half percent to their retirement allowances in July 2012. Also, there was an increase of 1,312 members and beneficiaries on the retired payroll as of June 30, 2013.

OTHER POST EMPLOYMENT BENEFIT ACTIVITIES

During the 2013 fiscal year, the medical insurance plan member contributions increased $19.5 million and employer contributions decreased $7.4 million from fiscal year 2012. The member contributions increased primarily due to the implementation of the Shared Responsibility Plan beginning July 1, 2010 which includes increased contributions from active and retired members, employers and the state. The employer contributions decreased due to less transition funding paid by the state as the Shared Responsibility plan phases in until the 2016 fiscal year. The state's contribution for the fiscal year was made with bond proceeds received in March 2013.

Net investment income increased $34.7 million from a negative $4.0 million in 2012 to $30.7 million in 2013. In 2011, net investment income totaled $8.3 million. This can be illustrated as follows:

Dollar Amount in Millions

	2013	**2012**	**2011**
Appreciation (depreciation) in fair value of investments – June 30, prior year	(9.7)	$ 0	$ 0
Appreciation (depreciation) in fair value of investments – June 30 end of year	15.7	(9.7)	0
Change in net appreciation(depreciation) in fair value of investments	25.4	(9.7)	0
Net income (net of investment expense)	5.3	6.0	8.3
Net gain (loss) on sale of investments	0	(0.3)	0
Investment Income (net) – June 30	$ 30.7	$ (4.0)	$ 8.3

The life insurance plan has an actuarial valuation conducted independently from the defined benefit plan. Total life insurance benefits paid for 2013, 2012 and 2011 were $4.6, $4.4, and $4.2 million respectively.

HISTORICAL TRENDS

Accounting standards require that the Statement of Plan Net Position state asset value at fair value and include only benefits and refunds due plan members and beneficiaries and accrued investment and administrative expenses as of the reporting date. Information regarding the actuarial funding status of the defined benefit plan, the medical insurance plan, and the life insurance plan is provided in the Schedule of Funding Progress (beginning on page 50). The asset value, stated in the Schedule of Funding Progress, is determined by the System's independent actuary. The actuarial accrued liability is calculated using the entry age cost method.

The 2013 fiscal year reveals a decline in funding position of the retirement annuity plan due primarily to an increase in the actuarial liability while the actuarial value of the assets remained flat due to market decline in prior years. Annual required employer contributions of the defined benefit plan are provided in the Schedule of Employer Contributions (on page 50) and a shortfall of employer contributions has resulted in an accumulated net pension obligation of $682,450,008 as of June 30, 2013.

Although the medical insurance plan continues to have a large unfunded actuarial liability, the current obligations are being met by current funding. Effective July 1, 2010 the Shared Responsibility Plan for funding retiree health benefits requires members, retirees, participating employers and the state to make contributions for pre-funding retiree medical benefits. Annual required contributions of the medical insurance plan are provided in the Schedule of Employer Contributions (on page 51) and a shortfall of employer contributions has resulted in an accumulated net OPEB obligation of $1,469,685,047 as of June 30, 2013.

Statement of Plan Net Position
As of June 30, 2013

	Defined Benefit Plan	Medical Insurance Plan	Life Insurance Plan	Other Funds	TOTAL
ASSETS					
Cash	$ 26,650,916	$ 6,879,174	$ 226,483	$ 68,943	$ 33,825,516
Prepaid Expenses	125,364	147,000			272,364
Receivables					
Contributions	38,461,507	9,771,489	22,945		48,255,941
Due From Other Trust Funds	1,300,238				1,300,238
State of Kentucky	31,975,561	3,350,147	69,683		35,395,391
Investment Income	48,247,677	1,375,970	1,039,330	1,607	50,664,584
Investment Sales Receivable	52,391,569	2,348,249			54,739,818
Other Receivables	656,500				656,500
Total Receivables	173,033,052	16,845,855	1,131,958	1,607	191,012,472
Investments at Fair Value (See Note 5)					
Short-Term Investments	796,485,774	56,915,874	1,907,900	541,819	855,851,367
Bonds and Mortgages	3,093,270,830	64,728,260	86,715,442	238,626	3,244,953,158
Equities	10,102,552,862	243,022,751		120,315	10,345,695,928
Alternative Investments	540,739,121	1,255,715			541,994,836
Real Estate	642,611,173				642,611,173
Additional Categories	882,969,785	83,487,054			966,456,839
Total Investments	16,058,629,545	449,409,654	88,623,342	900,760	16,597,563,301
Invested Security Lending Collateral	464,229,713				464,229,713
Capital Assets, at cost net of accumulated depreciation of $2,536,306 (See Note 2)	9,249,324				9,249,324
Total Assets	16,731,917,914	473,281,683	89,981,783	971,310	17,296,152,690
LIABILITIES					
Accounts Payable	1,513,830	4,058,236			5,572,066
Due to Other Trust Funds		1,275,206	24,425	607	1,300,238
Insurance Claims Payable		137,000			137,000
Revenues Collected in Advance		49,373,905			49,373,905
Investment Purchases Payable	157,366,066	4,771,571			162,137,637
Obligations Under Securities Lending	464,229,713				464,229,713
Total Liabilities	623,109,609	59,615,918	24,425	607	682,750,559
NET POSITION-RESTRICTED FOR PENSION AND OTHER POST-EMPLOYMENT BENEFITS:	$ 16,108,808,305	$ 413,665,765	$ 89,957,358	$ 970,703	$ 16,613,402,131

The combining statement of "Plan Net Position - Other Funds" is presented on page 26.
The accompanying notes are an integral part of these financial statements.

Statement of Plan Net Position
As of June 30, 2012

	Defined Benefit Plan	Medical Insurance Plan	Life Insurance Plan	Other Funds	TOTAL
ASSETS					
Cash	$ 25,314,512	$ $5,202,577	$ 299,153	$ 9,828	$ 30,826,070
Prepaid Expenses	62,774	147,000			209,774
Receivables					
Contributions	37,851,376	5,574,370	31,987		43,457,733
Due From Other Trust Funds	2,432,980				2,432,980
State of Kentucky	9,162,962	5,714,136	21,590		14,898,688
Investment Income	50,642,735	1,177,984	1,066,325	1,183	52,888,227
Investment Sales Receivable	33,559,535				33,559,535
Other Receivables	499,433	3,873,520			4,372,953
Total Receivables	134,149,021	16,340,010	1,119,902	1,183	151,610,116
Investments at Fair Value (See Note 5)					
Short-Term Investments	608,260,247	57,658,400	4,521,129	673,015	671,112,791
Bonds and Mortgages	3,209,187,529	87,375,468	86,345,459	270,532	3,383,178,988
Equities	9,259,302,459	140,740,862			9,400,043,321
Alternative Investments	451,266,337	748,103			452,014,440
Real Estate	586,800,766				586,800,766
Aditional Categories	586,106,748	53,027,854			639,134,602
Total Investments	14,700,924,086	339,550,687	90,866,588	943,547	15,132,284,908
Invested Security Lending Collateral	396,546,893				396,546,893
Capital Assets, at cost net of accumulated depreciation of $2,202,905 (See Note 2)	6,858,662				6,858,662
Total Assets	15,263,855,948	361,240,274	92,285,643	954,558	15,718,336,423
LIABILITIES					
Accounts Payable	4,052,099	3,762,868			7,814,967
Due to Other Trust Funds		2,387,658	44,397	925	2,432,980
Insurance Claims Payable		67,000			67,000
Revenues Collected in Advance		6,153,310			6,153,310
Investment Purchases Payable	66,136,067	10,122,885			76,258,952
Obligations Under Securities Lending	396,546,893				396,546,893
Total Liabilities	466,735,059	22,493,721	44,397	925	489,274,102
NET POSITION-RESTRICTED FOR PENSION AND OTHER POST-EMPLOYMENT BENEFITS:	$ 14,797,120,889	$ 338,746,553	$ 92,241,246	$ 953,633	$ 15,229,062,321

The combining statement of "Plan Net Position - Other Funds" is presented on page 27.
The accompanying notes are an integral part of these financial statements.

Statement of Changes in Plan Net Position
For the Year Ended June 30, 2013

	Defined Benefit Plan	Medical Insurance Plan	Life Insurance Plan	Other Funds	TOTAL
ADDITIONS					
Contributions					
Employer	$ 568,233,446	$ 166,576,444	$ 1,680,495	$ 140,000	$ 736,630,385
Member	304,738,728	119,795,780			424,534,508
Total Contributions	872,972,174	286,372,224	1,680,495	140,000	1,161,164,893
Other Income					
Recovery Income		34,976			34,976
Total Other Income		34,976			34,976
Investment Income					
Net Appreciation/(Depreciation) in FV of Investments	1,601,781,093	25,431,394	(2,822,147)	(18,885)	1,624,371,455
Interest	254,918,477	5,822,532	3,496,517	9,684	264,247,210
Dividends	184,104,556	20,949		1,507	184,127,012
Rental Income, Net	30,059,686				30,059,686
Securities Lending, Gross Earnings	3,077,116		390	3	3,077,509
Gross Investment Income	2,073,940,928	31,274,875	674,760	(7,691)	2,105,882,872
Less Investment Expense	(33,143,497)	(556,039)			(33,699,536)
Less Securities Lending Expense	(923,168)				(923,168)
Net Investment Income	2,039,874,263	30,718,836	674,760	(7,691)	2,071,260,168
Total Additions	2,912,846,437	317,126,036	2,355,255	132,309	3,232,460,037
DEDUCTIONS					
Benefits	1,570,722,924		4,614,718	114,632	1,575,452,274
Refunds of Contributions	22,059,094				22,059,094
Insurance Expenses		240,931,618			240,931,618
Administrative Expense	8,377,003	1,275,206	24,425	607	9,677,241
Total Deductions	1,601,159,021	242,206,824	4,639,143	115,239	1,848,120,227
Net Increase (Decrease)	1,311,687,416	74,919,212	(2,283,888)	17,070	1,384,339,810
NET POSITION-RESTRICTED FOR PENSION AND OTHER POST-EMPLOYMENT BENEFITS:					
Beginning of year	14,797,120,889	338,746,553	92,241,246	953,633	15,229,062,321
Ending of year	$16,108,808,305	$ 413,665,765	$ 89,957,358	$ 970,703	$ 16,613,402,131

The combining statement of "Changes in Plan Net Position - Other Funds" is presented on page 26.
The accompanying notes are an integral part of these financial statements.

Statement of Changes in Plan Net Position
For the Year Ended June 30, 2012

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

The combining statement of "Changes in Plan Net Position - Other Funds" is presented on page 27.
The accompanying notes are an integral part of these financial statements.

Combining Statement of Plan Net Position
as of June 30, 2013
OTHER FUNDS

	403(B) Tax Shelter	Supplemental Benefit Fund	Losey Scholarship	TOTAL
Assets				
Cash	$	$ 68,943	$	$ 68,943
Receivables				
Investment Income			1,607	1,607
Investments at Fair Value				
Short Term Investments	391,095		150,724	541,819
Bonds and Mortgages			238,626	238,626
Equities			120,315	120,315
Total Investments	391,095		509,665	900,760
Total Assets	391,095	68,943	511,272	971,310
Liabilities				
Due to Other Trust Funds	76	425	106	607
Net Position - Restricted for Pension and Other Post-Employment Benefits	$ 391,019	$ 68,518	$ 511,166	$ 970,703

Combining Statement of Changes in Plan Net Position
as of June 30, 2013
OTHER FUNDS

	403(B) Tax Shelter	Supplemental Benefit Fund	Losey Scholarship	TOTAL
Additions				
Contributions				
Employer	$	$ 140,000	$	$ 140,000
Investment Income/(Loss)				
Net Appreciation/(Depreciation) in Fair Value of Investments			(18,885)	(18,885)
Interest	448		9,236	9,684
Dividends			1,507	1,507
Securities Lending, Net			3	3
Net Investment Income/(Loss)	448		(8,139)	(7,691)
Total Additions	448	140,000	(8,139)	132,309
Deductions				
Benefits	14,260	80,372	20,000	114,632
Administrative Expense	76	425	106	607
Net Increase (Decrease)	(13,888)	59,203	(28,245)	17,070
Net Position - Restricted for Pension and Other Post-Employment Benefits				
Beginning of Year	404,907	9,315	539,411	953,633
End of Year	$ 391,019	$ 68,518	$ 511,166	$ 970,703

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

Combining Statement of Plan Net Position
as of June 30, 2012
OTHER FUNDS

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

Combining Statement of Changes in Plan Net Position
as of June 30, 2012
OTHER FUNDS

	403(B) Tax Shelter	Supplemental Benefit Fund	Losey Scholarship	TOTAL
Additions				
Contributions				
Employer	$	$	$	$
Investment Income/(Loss)				
Net Appreciation/(Depreciation) in Fair Value of Investments			66,220	66,220
Interest	713		9,310	10,023
Net Investment Income/(Loss)	713		75,530	76,243
Total Additions	713		75,530	76,243
Deductions				
Benefits	18,952	55,280	18,000	92,232
Administrative Expense	99	287	94	480
Net Increase (Decrease)	(18,338)	(55,567)	57,436	(16,469)
Net Position - Restricted for Pension and Other Post-Employment Benefits				
Beginning of Year	423,245	64,882	481,975	970,102
End of Year	$ 404,907	$ 9,315	$ 539,411	$ 953,633

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

Notes to Financial Statements
Years Ended June 30, 2013 and 2012

Note 1: Description of Retirement Annuity Plan

A. REPORTING ENTITY

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

B. PARTICIPANTS

As of June 30, 2013 a total of 208 employers participated in the plan. Employers are comprised of local school districts, Department of Education Agencies, universities, the Kentucky Community and Technical College System, and other educational organizations.

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

	2013	2012
Active contributing members:		
Vested	48,620	48,383
Non-vested	26,211	27,568
Inactive members, vested	7,194	6,668
Retirees and beneficiaries currently receiving benefits	47,406	46,094
Total members, retirees, and beneficiaries	**129,431**	**128,713**

C. BENEFIT PROVISIONS

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

1.) Attain age fifty-five (55) and complete five (5) years of Kentucky service, or
2.) Complete 27 years of Kentucky service.

Participants that retire before age sixty (60) with less than twenty-seven (27) years of service receive reduced retirement benefits. Non-university members receive monthly payments equal to two percent (2%) (service prior to July 1, 1983) and two and one-half percent (2.5%) (service after July 1, 1983) of their final average salaries for each year of credited service. University employees receive monthly benefits equal to two percent (2%) of their final average salary for each year of credited service. The final average salary is the member's five (5) highest annual salaries except members at least age fifty-five (55) with twenty-seven (27) or more years of service may use their three (3) highest annual salaries. New members (including second retirement accounts started) after July 1, 2002 will receive monthly benefits equal to two percent (2%) of their final average salary for each year of service if, upon retirement, their total service is less than ten (10) years. New members after July 1, 2002 who retire with ten (10) or more years of total service will receive monthly benefits equal to two and one-half percent (2.5%) of their final average salary for each year of service, including the first ten (10) years. In addition, non-university members who retire July 1, 2004 and later with more than thirty (30) years of service will have their multiplier increased for all years over thirty (30) from two and one-half percent (2.5%) to three percent (3%) to be used in their benefit calculation.

Note 1: Description of Retirement Annuity Plan continued . . .

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

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

Note 2: Summary of Significant Accounting Policies

A. BASIS OF ACCOUNTING

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

B. CASH

KTRS has five cash accounts. At June 30, 2013, the retirement annuity cash account totaled $25,651,419 and the administrative expense fund cash account was $999,497 for a total of $26,650,916 as carrying value of cash in the defined benefit plan. The medical insurance cash account totaled $6,879,174, the life insurance plan cash account totaled $226,483 and the excess benefit fund cash account contained $68,943. Therefore, the carrying value of cash was $33,825,516 and the bank balance was $30,191,478 and funds controlled by the Commonwealth of Kentucky of $6,527,386. The variance is primarily due to outstanding checks and items not processed by the bank on June 30, 2013.

C. CAPITAL ASSETS

Fixed assets are recorded at historical cost less straight-line accumulated depreciation. The classes of fixed assets are furniture and equipment, the KTRS office buildings and land. Furniture and equipment are depreciated over an average useful life of five (5) years. The office buildings are depreciated over forty years. The Pathway System will be capitalized and amortized or depreciated over ten years. The Pathway System will replace KTRS's legacy computer system and be KTRS's primary line of business information technology system. As of June 30, 2013, the project to build and implement the Pathway System was approximately fifty percent (50%) complete.

D. INVESTMENTS

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

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

E. COMPENSATED ABSENCES

Expenses for accumulated vacation days and compensatory time earned by the System's employees

Note 2: Summary of Significant Accounting Policies continued . . .

are recorded when earned. Upon termination or retirement, employees of the System are paid for accumulated vacation time limited to sixty (60) days and accumulated compensatory time limited to two hundred-forty (240) hours. As of June 30, 2013 and 2012 accrued compensated absences were $979,037 and $876,573.

F. RISK MANAGEMENT

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

G. OTHER RECEIVBLES

KTRS allows qualified purchases of service credit to be made by installment payments not to exceed a five (5) year period. Revenue is recognized in the initial year of the installment contract agreement. The June 30, 2013 and 2012 installment contract receivables were $656,500 and $499,433.

H. USE OF ESTIMATES

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

I. INCOME TAXES

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

J. RECENT PRONOUNCEMENTS

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

In April 2012, GASB issued Statement No. 65, Items Previously Reported as Assets and Liabilities. This pronouncement clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. GASB Statement No. 65 is effective for fiscal years beginning after December 15, 2012 (the fiscal year ended June 30, 2014). The impact of this statement on the financial statements has not yet been determined.

In June 2012, the GASB issued Statement No. 67, Financial Reporting for Pension Plans and Statement No. 68, Accounting and Financial Reporting for Pensions. GASB Statement No. 67 replaces GASB Statement No. 25, Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans. GASB Statement No. 68 replaces GASB Statement No. 27, Accounting for Pensions by State and Local Governmental Employers. GASB Statement No. 67 is effective for the year ending June 30, 2014, and GASB Statement No. 68 will be effective for the year ending June 30, 2015. At this time, *Note 2: Summary of Significant Accounting Policies continued . . .*

management is reviewing the recently issued pronouncements to determine the impact on KTRS's financial statements. An additional report related to GASB Statement No. 67 can be found beginning on page 139 in the Actuarial section of this CAFR.

K. RECLASSIFICATIONS

Certain 2012 amounts have been reclassified in conformity with the 2013 presentation.

Note 3: Contributions and Reserves

A. CONTRIBUTIONS

Contribution rates are established by Kentucky Revised Statutes. Non-university members are required to contribute 10.855 percent of their salaries to the System; university members are required to contribute 9.055 percent of their salaries. KRS 161.565 allows each university to reduce the contribution of its members by 2.215 percent; therefore, university members contribute 6.840 percent of their salary to KTRS. University members who joined the plan on and after July 2008 are required to contribute an additional .32 percent to the medical insurance plan.

For members employed by local school districts, the state contributes 13.105 percent of salary for those who joined before July 1, 2008 and 14.105 percent for those who joined thereafter.

Other participating employers are required to contribute the percentage contributed by members plus an additional 3.25 percent of members' gross salaries.

The member and employer contributions consist of retirement annuity contributions and other post-employment benefit contributions to the medical and life insurance plans. The member post-employment medical contribution is 1.75 percent. The employer post-employment medical contribution is .75 percent of member gross salaries. Also, after July 1, 2010 employers (other than the state) contribute 1.0 percent of members' salaries and the state contributes the net cost of health insurance premiums for new retirees after June 30, 2010 in the non-Medicare eligible group. If a member leaves covered employment before accumulating five (5) years of credited service, accumulated member contributions to the retirement annuity plan plus interest are refunded upon the member's request.

B. RESERVES

Member Reserve

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

Employer Reserve

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

Benefit Reserve

This fund was established by KRS 161.420(4) as the Allowance Reserve Fund, the source for retirement, disability, and survivor benefits paid to members of the System. These benefits are paid from the retired members' contributions until they are exhausted, at which time state matching contributions are used to

Note 3: Contributions and Reserves continued . . .

pay the benefits. After an individual member's contributions and the state matching contributions have been exhausted, retirement benefits are paid from monies transferred from Unallocated Reserves.

Unallocated Reserve

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

Administrative Expense Reserve

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

Note 4: Funded Status and Funding Progress

A. DESCRIPTION OF FUNDING PROGRESS

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

Schedule of Funding Progress
(Dollar amount in thousands)

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liabilities	Unfunded Actuarial Accured Liabilities (UAAL)	Funded Ratio	Covered Payroll	UAAL As a % of Covered Payroll
	A	B	(B-A)	(A/B)	C	[(B-A)/C]
6/30/2013	$ 14,962,758	$ 28,817,232	$ 13,854,474	51.9%	$ 3,480,066	398.1%

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

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

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

Note 4: Funded Status and Funding Progress continued . . .

B. METHODOLOGIES

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

Actuarial Value of Assets

(1)	Actuarial Value of Assets on June 30, 2012			$ 14,691,371,043
(2)	Market Value End of Year June 30, 2013			16,108,808,305
(3)	Market Value Beginning of Year June 30, 2012			14,797,120,889
(4)	Cash Flow			
		a.	Contributions (exclusive of Pension Obligation Bond)	872,972,174
		b.	Benefit Payments	(1,592,782,018)
		c.	Administrative Expenses	(8,377,003)
		d.	Net	(728,186,847)
(5)	Investment Income			
		a.	Market total: (2) - (3) -(4)d	2,039,874,263
		b.	Assumed Rate	7.5%
		c.	Amount for Immediate Recognition: [(3) x (5)b] + [(4)d * (5)b * 0.5]	1,082,477,060
		d.	Amount for Phased-In Recognition: (5)a - (5)c	957,397,203
(6)	Phased-In Recognition of Investment Income			
		a.	Current Year: 0.20 x (5)d	191,479,441
		b.	First Prior Year	(160,195,981)
		c.	Second Prior Year	363,670,625
		d.	Third Prior Year	133,378,916
		e.	Fourth Prior Year	(611,235,941)
		f.	Total Recognized Investment Gain	(82,902,940)
(7)	Actuarial Value End of Year		(1) + (4)d + (5)c +(6)f	14,962,758,316
(8)	Difference Between Market & Actuarial Values: (2) - (7)			$ 1,146,049,989
(9)	Rate of Return on Actuarial Value			6.98%

C. ASSUMPTIONS

Significant actuarial assumptions employed by the actuary for the funding purposes as of June 30, 2013, the most recent updated actuarial information include:

*	Assumed inflation rate	3.50%
*	Assumed investment rate	7.50%
*	Assumed projected salary increases	4.00% - 8.20%
*	Assumed annual cost of living adjustments	1.50%

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements)

A. LEGAL PROVISIONS FOR INVESTMENTS

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

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

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

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

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

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

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

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

B. CASH AND CASH EQUIVALENTS

For cash deposits and cash equivalents, custodial credit risk is the risk that, in the event of a bank failure, the retirement system's deposits may not be returned to the system. The retirement system's total cash balance held at J.P. Morgan Chase Bank in noninterest-bearing accounts on June 30, 2013 was $30,191,478. In addition to these funds, an amount of $6,527,386 represents funds transferred to and controlled by the Commonwealth of Kentucky.

On November 9, 2010, the FDIC issued a Final Rule implementing Section 343 of the Dodd-Frank Wall Street Reform and Consumer Protection Act that provides for unlimited insurance coverage of noninterest-bearing transaction accounts. Beginning December 31, 2010, through December 31, 2012, all noninterest-bearing transaction accounts are fully insured, regardless of the balance of the account, at all FDIC-insured institutions. Therefore, all cash balances were fully insured by the FDIC through December 31, 2012. Beginning January 1, 2013, all cash balances at J.P. Morgan Chase Bank were insured up to $250,000 and the remaining balances fully collateralized with securities held by the Federal Reserve Bank of New York in the name of the Commonwealth of Kentucky-Teachers' Retirement.

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

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

As of June 30, 2013, the retirement system's cash balance in the amount of $30,191,478 was not exposed to custodial credit risk since this amount was fully insured by the FDIC limit of $250,000 and the remaining balances collateralized with securities valued at $42,467,757.

C. INVESTMENTS

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

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

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

The following chart represents the fair values of the investments of the Kentucky Teachers' Retirement System for June 30, 2013.

Schedule of Investments
Retirement Annuity Trust

	Fair Value June 30, 2013	Fair Value June 30, 2012
Money Market Fund	$ 766,568,843	$ 625,060,870
Commercial Paper	34,560,147	
Total Cash Equivalents*	**801,128,990**	**625,060,870**
U.S. Government	650,217,435	502,533,682
Agency Bonds	146,127,074	156,932,114
Mortgage Backed Securities	180,378,637	199,128,064
Asset Backed Securities	41,175,017	60,608,480
Commercial Mtg Backed Securities	210,980,212	295,709,822
Collateralized Mtg Obligations	41,523,706	43,276,306
Municipal Bonds	460,132,862	511,018,984
Corporate Bonds	1,449,689,955	1,526,596,068
Total Fixed Income	**3,180,224,898**	**3,295,803,520**
Global		
International Equity	2,676,211,485	2,307,653,944
U.S. Equity	7,426,461,692	6,951,648,515
Total Equities	**10,102,673,177**	**9,259,302,459**
Real Estate Equity	642,611,173	586,800,766
Total Real Estate Equity	**642,611,173**	**586,800,766**
Private Equity	343,259,092	265,833,651
Timberland	197,480,029	185,432,686
Total Alternative Investments	**540,739,121**	**451,266,337**
Opportunistic Credit	477,554,833	191,846,044
Corporate	307,715,989	271,894,458
International Bonds	91,778,981	
PPIP	4,859,928	121,357,075
Preferred US Equity	1,060,054	1,009,171
Total Additional Categories	**882,969,785**	**586,106,748**
TOTAL INVESTMENTS	**$ 16,150,347,144**	**$ 14,804,340,700**

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

Schedule of Investments Comparison
Health Insurance Trust

	Fair Value June 30, 2013	Fair Value June 30, 2012
Money Market Fund	$ 54,722,377	$ 46,051,921
Total Cash Equivalents	**54,722,377**	**46,051,921**
Agency Bonds	32,292,470	87,375,468
Asset Backed Securities	9,360,161	
Corporate Bonds	23,075,629	52,755,524
Total Fixed Income	**64,728,260**	**140,130,992**
Global	243,022,751	140,740,862
Total Equities	**243,022,751**	**140,740,862**
Private Equity	1,255,715	748,103
Total Alternative Investments	**1,255,715**	**748,103**
Opportunistic Credit	23,840,109	
Corporate	59,360,240	
Preferred US Equity	286,705	272,330
Total Additional Categories	**83,487,054**	**272,330**
Total Investments	**$ 447,216,157**	**$ 327,944,208**

Custodial Credit Risk

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

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

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

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

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

As of June 30, 2013, cash collateral reinvestment securities acquired through securities lending for the retirement annuity trust fund by KTRS's custodian, who is also the lending agent/counterparty, amounted to $464,229,713 related to $450,695,509 securities lent consistent with the lending agreement with the custodian. (Please refer to a following section entitled Securities Lending.)

Interest Rate Risk

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

As of June 30, 2013, the retirement annuity trust and health insurance trusts had the following investments and weighted average maturities:

Retirement Annuity Trust

Investment Type	Fixed Income	Additional Categories	Average Maturity (years)
U.S. Government	$ 650,217,435	$	8.36
Agency	146,127,074		8.41
MBS	180,378,637		13.76
CMO	41,523,706		18.63
ABS	41,175,017		15.30
CMBS	210,980,212		25.70
Muni	460,132,862	53,077,891	13.11
Corporate	1,449,689,955	522,504,400	7.95
Totals	**$ 3,180,224,898**	**$ 575,582,291**	**10.22**

Health Insurance Trust

Investment Type	Fixed Income	Additional Categories	Average Maturity (years)
Agency	$ 32,292,470	$	6.05
ABS	9,360,161		1.20
Corporate	23,075,629	82,069,081	5.65
Totals	**$ 64,728,260**	**$ 82,069,081**	**5.45**

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

In addition to the above securities, the System held short-term cash investments in the Dreyfus Institutional Cash Advantage Fund and STIF, held at the Bank of New York Mellon, with a total fair value of $821,291,220 and had a weighted average maturity of forty-one (41) days. Average maturity is used as a measure of a security's exposure to interest rate risk due to fluctuations in market interest rates. Mortgage-backed securities and collateralized mortgage obligations are typically amortizing investments with an average life and interest rate risk significantly less than suggested by the legal maturity. Mortgage-backed securities, which are generally pre-payable, and other callable bonds are subject to adverse changes in average life in response to market interest rate changes. The schedule above reflects only the legal maturity of all such bonds.

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

Mortgage-backed securities are securities representing pass-through interests in the cash flows from pools of mortgage loans on single-family or multi-family residential properties. All of the mortgage-backed securities owned by the retirement system were securitized and are guaranteed by Fannie Mae, Freddie Mac, or GNMA. The average life of a mortgage-backed security depends upon the level of prepayments experienced in the underlying pool of loans. Market interest rates are a primary determinant of prepayment levels. Lower than anticipated market rates generally lead to higher than anticipated prepayments and a shorter average life; higher than anticipated market rates generally lead to lower than anticipated prepayments and a longer average life. The retirement system held $180.4 million in mortgage-backed securities as of June 30, 2013.

Collateralized mortgage obligations are bonds that are collateralized by whole loan mortgages, mortgage pass-through securities or stripped mortgage-backed securities. Income is derived from payments and prepayments of principal and interest generated from collateral mortgages. Cash flows are distributed to different investment classes in accordance with a collateralized mortgage obligations established payment order. The System held $41.5 million in collateralized mortgage obligations as of June 30, 2013.

Asset-backed securities are bonds or notes backed by loan paper or accounts receivables originated by banks, credit card companies, or other credit providers, and are considered to be moderately sensitive to changes in interest rates. The originator of the loan or accounts receivable paper sells it to a specially created trust, which repackages it as securities. Asset-backed securities have been structured as pass-throughs and as structures with multiple bond classes. The retirement annuity trust held $41.2 million, and the health insurance trust held $9.4 million in asset backed securities as of June 30, 2013.

Commercial mortgage-backed securities are securities representing interests in the cash flows from pools of mortgage loans on commercial properties. The interests in a securitized pool of loans are generally divided into various tranches based upon planned payment order and level of seniority. The retirement system's commercial mortgage-backed securities investments consist of highly rated relatively senior tranches. The average maturity of the retirement system's commercial mortgage-backed securities holdings in the schedule above reflects the legal maturity of those holdings. Most of the tranches held are earlier in the planned payment order than the legal maturity suggests. The retirement system held $211.0 million in commercial mortgage-backed securities investments as of June 30, 2013.

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

Credit Risk

Credit risk is the risk that an issuer or counterparty to an investment will not fulfill its obligations. The following schedule lists KTRS's fixed income investments (net of cash equivalents) according to credit ratings as of June 30, 2013:

Retirement Annuity Trust

Rating	Bonds & Mortgages	Additional Categories	Total	%
U.S. Government	$ 650,217,435	$	$ 650,217,435	17.31
AAA	395,149,816	21,149,744	416,299,560	11.08
AA	887,644,553	23,525,750	911,170,303	24.26
A	691,886,217	32,343,439	724,229,656	19.29
BBB	520,466,142	36,753,231	557,219,373	14.84
BB	13,617,750	207,935,099	221,552,849	5.90
B	11,260,000	226,575,403	237,835,403	6.33
CCC		21,397,284	21,397,284	0.57
D		722,240	722,240	0.02
Not Rated	9,982,985	5,180,101	15,163,086	0.40
Total	**$ 3,180,224,898**	**$ 575,582,291**	**$ 3,755,807,189**	**100.00**%

Health Insurance Trust

Rating	Bonds & Mortgages	Additional Categories	Total	%
AAA	$ 9,360,161	$	$ 9,360,161	6.38
AA	33,782,961		33,782,961	23.01
A	21,585,138	258,390	21,843,528	14.88
BBB		5,683,810	5,683,810	3.88
BB		32,396,397	32,396,397	22.07
B		40,562,606	40,562,606	27.63
CCC		2,790,659	2,790,659	1.90
D		152,500	152,500	0.10
Not Rated		224,719	224,719	0.15
Total	**$ 64,728,260**	**$ 82,069,081**	**$ 146,797,341**	**100.00**%

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

Total fair value of the retirement annuity trust's fixed income portfolio was $3,755,807,189 on June 30, 2013. The health insurance trust's fixed income portfolio was valued at $146,797,341. The rating system used in the above charts is the Standard and Poor's rating system. For securities where a Standard and Poor's rating is not provided, another nationally recognized system is used and translated to the Standard and Poor's rating system.

In addition to the above categories, the retirement annuity trust held $766,568,843 in short term investments through the Dreyfus Institutional Cash Advantage Fund, and $34,560,147 in short term commercial paper. The health insurance trust held $54,722,377 in the Dreyfus Institutional Cash Advantage Fund. The credit risk associated with this Fund is minimal as the securities held are required to maintain the highest possible short-term credit ratings by Moody's and Standard & Poor's. In addition, investments in US Government and Agency securities are also highly rated securities since they are backed by the US Government. Notation is made that the ratings of securities is subject to change due to circumstances and thereby may have a lower rating than when first purchased.

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

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

Concentration of Credit Risk

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

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

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

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

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. As of June 30, 2013, the retirement system's exposure to foreign currency risk consisted of $3,095,845,767 and $150,873,788 in the retirement annuity trust and health insurance trust funds respectively.

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

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

Retirement Annuity Trust

Commingled Funds	
Rogge Global Int'l Fixed Income	$ 73,866,899
Baillie Gifford Intrntl EAFE	621,831,309
Baring All Country World ex US	445,951,918
BlackRock ACWI EX-US IMI	350,243,165
UBS All Country World ex US	471,191,694
Alternative Funds	
KKR & Co. European Fund III	56,543,955
Oaktree European Principal Fund III	10,157,366
ADRs (Equities)	742,298,527
Bonds (Fixed Income)	263,935,728
Additional Categories (Fixed Income)	59,825,206
Total	**$ 3,095,845,767**

Health Insurance Trust

Commingled Funds	
Medical Ins. Black Rock Fund B	$ 123,779,544
Bonds (Fixed Income)	16,494,738
Additional Categories (Fixed Income)	10,599,506
Total	**$ 150,873,788**

The following tables reflect the various foreign currencies associated with the System's investments in the funds outlined previously:

Retirement Annuity Trust

Currency	Market Value	Currency	Market Value
Australian Dollar	$ 139,445,987	Liberian Dollar	623,428
Bermudian Dollar	25,839,445	Malaysian Ringgit	11,754,031
Bolívar Fuerte	4,073,160	Mexican Peso	38,235,293
Brazilian Real	55,494,528	Moroccan Dirham	55,074
British Pound Sterling	444,596,277	New Zealand Dollar	4,849,609
Canadian Dollar	251,933,687	Norwegian Krone	31,375,502
Cayman Islands Dollar	21,138,551	Panamanian Balboa	12,456,400
Chilean Peso	3,943,914	Peruvian Nuevo Sol	9,007,698
Chinese Yuan	129,822,181	Philippine Peso	813,813
Colombian Peso	6,597,535	Polish Zloty	8,464,289
Czech Crown	215,546	Riyal	873,676
Danish Krone	39,745,423	Russian Ruble	70,082,989
Dominican Peso	293,074	Singapore Dollar	45,740,231
Egyptian Pound	236,259	South African Rand	16,219,538
Euro	688,338,617	South Korean Won	74,639,548
Hong Kong Dollar	72,220,920	Swedish Krona	106,734,326
Hungarian Forint	181,169	Swiss Franc	238,386,117
Indian Rupee	29,461,493	Taiwan Dollar	47,424,825
Indonesian Rupiah	5,784,260	Thai Baht	9,219,788
Israeli New Shekel	35,107,147	Turkish Lira	12,314,086
Japanese Yen	378,471,443	Various	5,391,439
Jersey Pound	18,029,727		
Kuna	213,724	**Total**	**$ 3,095,845,767**

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

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

Health Insurance Trust

Currency	Market Value	Currency	Market Value
Australian Dollar	$ 7,313,118	Mexican Peso	1,360,770
Brazilian Real	2,911,930	Moroccan Dirham	20,324
British Pound Sterling	19,024,292	New Zealand Dollar	196,583
Canadian Dollar	16,175,326	Norwegian Krone	872,933
Cayman Islands Dollar	1,158,038	Peruvian Nuevo Sol	7,294
Chilean Peso	510,183	Philippine Peso	300,096
Chinese Yuan	99,323	Polish Zloty	408,204
Colombian Peso	277,911	Russian Ruble	1,082,483
Czech Crown	59,223	Singapore Dollar	1,588,529
Danish Krone	1,548,560	South African Rand	1,977,658
Egyptian Pound	85,039	South Korean Won	4,020,630
Euro	38,158,584	Swedish Krona	2,742,732
Hong Kong Dollar	7,348,663	Swiss Franc	9,812,335
Hungarian Forint	63,670	Taiwan Dollar	3,516,810
Indian Rupee	1,801,775	Thai Baht	809,220
Indonesian Rupiah	934,193	Turkish Lira	549,548
Israeli New Shekel	535,800	Various	1,873,527
Japanese Yen	20,474,487		
Liberian Dollar	114,660	**Total**	**$ 150,873,788**
Malaysian Ringgit	1,139,337		

The majority of foreign investments are held in commingled funds managed by Rogge Global Partners, UBS Global Asset Management, Baillie Gifford, Baring Asset Management, and Black Rock. In addition to the commingled funds investing in foreign securities, the retirement annuity trust fund held $742,298,527 associated with foreign interests in American Depositary Receipt investments. These American Depositary Receipts are securities that are issued by a U.S. bank in place of the foreign stock shares held in trust by that bank, thereby facilitating the trading of foreign shares in U.S. markets. American Depositary Receipts are denominated in U.S. currency. Other foreign securities and investments consisted of debt securities and alternative investment opportunities.

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

D. SECURITIES LENDING

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

Note 5: Deposits With Financial Institutions and Investments (Including Repurchase Agreements) continued . . .

Securities lending transactions are accounted for in accordance with GASB Statement No. 28 Accounting and Financial Reporting for Securities Lending Transactions, which established standards of accounting and financial reporting for securities lending transactions. During the fiscal year ended June 30, 2013, only the retirement annuity trust fund had securities lending transactions. The following section details the net income earned in the retirement annuity trust fund from securities lending for the fiscal year ended June 30, 2013:

Item	2013 Earnings	2012 Earnings
Gross Earnings (Interest and Fees)	$ 600,782	$ 314,708
Gross Borrower Rebates	2,476,727	2,790,509
Bank Fees	(923,168)	(931,520)
Net Earnings	**$ 2,154,341**	**$ 2,173,697**

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

As of June 30, 2013 the loan average days to maturity in the retirement annuity trust fund was one (1) days and the weighted average investment maturity of cash collateral investments was one (1) days. At fiscal year end, the retirement annuity trust fund had no credit risk exposure to borrowers, since the amounts the retirement annuity trust fund owes the borrowers exceeds the amounts the borrowers owe the retirement annuity trust fund and there were no losses resulting during the period.

Security lending programs can entail interest rate risk and credit risk. The retirement system minimizes interest rate risk by limiting the term of cash collateral investments to several days.

The credit risk is controlled by investing cash collateral in securities with qualities similar to the credit worthiness of lent securities.

The following table presents the fair values of the underlying securities, and the value of the collateral pledged at June 30, 2013:

Type of Security Lent	Fair Value	Cash & Non-Cash Collateral Value Received
Fixed Income	$ 274,689,711	$ 282,088,080
Equities	176,005,798	182,141,633
Total	**$ 450,695,509**	**$ 464,229,713**

Note 6: Retirement Plan for Employees of the System

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

The System's annual required contributions for KTRS employee members for the fiscal years 2013, 2012 and 2011 were $574,432, $533,378, and $469,896 respectively. KTRS contributed one hundred percent (100%) of the required contribution each year.

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

Members of KERS who joined prior to July 1, 2008, are required to contribute five percent (5%) of their annual creditable compensation for the fiscal years 2013, 2012 and 2011 and members who joined on or after July 1, 2008 contribute an additional one percent (1%). As the employer, KTRS is required to contribute the annual actuarially determined rate of the creditable compensation (or the rate approved by legislators). The approved rate for the fiscal years 2013, 2012 and 2011 were 23.61 percent, 19.82 percent and 16.98 percent and the System's annual required contributions to KERS were $331,989, $350,869, and $241,899 respectively. KTRS contributed one hundred percent (100%) of the required contributions for each year.

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

Note 7: Other Funds

A. 403(B) TAX-SHELTERED ANNUITY PLAN

__Plan Description__

KTRS has, in prior years, administered a salary deferral program as permitted by section 403(b) of the Internal Revenue Code. Under this program members were able to voluntarily defer a portion of their compensation within the limits established by the applicable laws and regulations. However, the System's Board of Trustees determined that the cost of providing the necessary services to assure the System of continuing compliance with these laws and regulations was not economically feasible due to the limited participation in the program by the System's members. The Board decided, therefore, to discontinue offering the program as of April 30, 1997. Members who were not receiving annuities from their account as of April 30, 1997, were able to transfer their respective accounts directly into other tax-sheltered plans on a tax-free basis. As of June 30, 2013, the twelve members who are receiving annuities will continue to receive distributions according to the terms of their respective elections.

Note 7: Other Funds continued . . .

B. SUMMARY OF SIGNIFICANT POLICIES

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

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

C. SUPPLEMENTAL BENEFIT FUND

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

D. JUNITA LOSEY SCHOLARSHIP BEQUEST

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

Note 8: Medical Insurance Plan & Post-Employment Benefits

A. PLAN DESCRIPTION

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

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

To be eligible for medical benefits, the member must have retired either for service or disability. The KTRS medical plan offers coverage to members under the age of 65 through the Kentucky Employees Health Plan administered by the Kentucky Department of Employee Insurance. KTRS retired members

Note 8: Medical Insurance Plan & Post-Employment Benefits continued . . .

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

At June 30, 2013, KTRS insurance covered 36,777 retirees and 7,053 dependents. There are 208 participating employers and 74,831 active members contributing to the medical plan.

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The KTRS medical plan financial statements are prepared using the accrual basis of accounting. Member contributions and employer matching are recognized in the fiscal year due.

Healthcare premiums charged to retired members are recognized when due and any premiums collected in advance are recognized as a liability.

Method Used to Value Investments

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

C. CONTRIBUTIONS

The post-employment medical benefit provided by KTRS is financed on a pre-funded basis beginning July 1, 2010 with the implementation of the "Shared Responsibility" legislation. In order to fund medical benefits, active member contributions are matched by the state at .75% of members' gross salaries. Members contributed 1.75% of gross payroll to the KTRS medical plan and beginning July 1, 2010 the contribution increases incrementally to 3.75% by July 1, 2015 under the Shared Responsibility Plan. Also, the premiums collected from retirees and investment income contributes to funding the plan. The KTRS medical plan received $152,400,000 in fiscal year 2013 in funding from the state, which was contributed to the insurance trust fund. This transitional funding and increased contributions are for the 2013 and 2014 fiscal years.

D. FUNDED STATUS AND FUNDING PROGRESS

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

Schedule of Funding Progress
(Dollar amount in thousands)

Actuarial Valuation Date	Actuarial Value of Assets A	Actuarial Accrued Liabilities B	Unfunded Actuarial Accured Liabilities (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll C	UAAL As a % of Covered Payroll [(B-A)/C]
6/30/2013	$ 412,185	$ 3,521,073	$ 3,108,888	11.7%	$ 3,480,066	89.3%

Note 8: Medical Insurance Plan & Post-Employment Benefits continued . . .

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

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

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

Significant actuarial methodologies and assumptions employed as of the June 30, 2013 valuation date include the following:

Actuarial Cost Method	Actuarial Value of Assets	Assumed Inflation Rate	Investment Rate of Return	Amortization Method	Remaining Amortization Period
Entry Age	Market value of assets	3.50%	8.00%	Level percent of pay, open	30 years

Medical Trend Assumption	Pre-Medicare	Medicare
Fiscal Year Ending 6/30/2014	8.50%	0.00%
Fiscal Year Ending 6/30/2015	7.50%	6.00%
Ultimate Trend Rate	5.00%	5.00%
Year of Ultimate Trend Rate	2019	2018

E. INCURRED BUT NOT REPORTED CLAIMS LIABILITIES

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

The following schedule shows the change in the claims and liability and the claims activity for the years ended June 30, 2013 and 2012.

Note 8: Medical Insurance Plan & Post-Employment Benefits continued . . .

	2013	2012
Beginning Unpaid Claims Liability	$ 67,000	$ 403,000
Current Year Claims and Changes in Estimates	196,676,714	189,926,846
Claims Payments	(196,606,714)	(190,262,846)
Ending Unpaid Claims Liability	**$ 137,000**	**$ 67,000**

Note 9: Life Insurance Plan

A. PLAN DESCRIPTON

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

B. SUMMARY OF SIGNIFICANT POLICIES

Basis of Accounting

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

Method Used to Value Investments

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

C. CONTRIBUTIONS

To finance the life insurance benefit a portion of the employer contribution rate is directed to the plan as recommended by the KTRS's actuary. For both fiscal years 2013 and 2012, this rate has been .05% of active members' payroll.

D. FUNDED STATUS AND FUNDING PROGRESS

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

Schedule of Funding Progress
(Dollar amount in thousands)

Actuarial Valuation Date	Actuarial Value of Assets A	Actuarial Accrued Liabilities (AAL) B	Unfunded Actuarial Accured Liabilities (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll C	UAAL As a % of Covered Payroll [(B-A)/C]
6/30/2013	$ 94,863	$ 94,325	$ (538)	100.6%	$ 3,480,066	(0.02)%

Note 9: Life Insurance Plan continued . . .

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. The required supplementary schedules following the notes to the financial section contain more actuarial information. Significant actuarial methodologies and assumptions employed as of the June 30, 2013 valuation date include the following:

Actuarial Cost Method	Actuarial Value of Assets	Assumed Inflation Rate	Investment Rate of Return	Projected Salary Increases	Amortization Method	Remaining Amortization Period
Entry Age	Market value of assets	3.50%	7.50%	4.00%	Level percent of pay, open	30 years

Required Supplementary Information

Defined Benefit Plan – Schedule of Funding Progress

(Dollar amount in thousands)

Actuarial Valuation Date	Actuarial Value of Assets A	Actuarial Accrued Liabilities (AAL) B	Unfunded Actuarial Accured Liabilities (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll C	UAAL as a % of Covered Payroll [(B-A)/C]
6/30/2008	$ 15,321.3	$ 22,460.3	$ 7,139.0	68.2%	$ 3,190.3	223.8%
6/30/2009	14,886.9	23,400.3	8,514.4	63.6	3,253.1	261.7
6/30/2010	14,851.3	24,344.3	9,493.0	61.0	3,321.6	285.8
6/30/2011	14,908.1	25,968.7	11,060.6	57.4	3,451.8	320.4
6/30/2012	14,691.4	26,973.9	12,282.5	54.5	3,479.6	353.0
6/30/2013	14,962.8	28,817.2	13,854.4	51.9	3,480.1	398.1

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

Defined Benefit Plan – Schedule of Employer Contributions

Fiscal Year Ended	Annual Required Contributions (A)	Actual Employer Contributions (B)	Percentage Contributed (B) / (A)
6/30/2008	$ 563,789,483	$ 466,247,783	83%
6/30/2009	600,282,735	442,549,935	74
6/30/2010	633,938,088	479,805,088	76
6/30/2011	678,741,428	1,037,935,993*	153
6/30/2012	757,822,190	557,339,552	74
6/30/2013	802,984,644	568,233,446	71

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

Note 9: Required Supplementary Information continued . . .

Medical Insurance Fund – Schedule of Funding Progress

(Dollar amount in millions)

Actuarial Valuation Date	Actuarial Value of Assets A	Actuarial Accrued Liabilities (AAL) B	Unfunded Actuarial Accured Liabilities (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll C	UAAL as a % of Covered Payroll [(B-A)/C]
6/30/2008	$ 185.9	$ 6,434.5	$ 6,248.6	2.9%	$ 3,190.3	195.9%
6/30/2009	229.1	6,454.7	6,225.6	3.5	3,253.1	191.4
6/30/2010	241.2	3,206.8	2,965.6	7.5	3,321.6	89.3
6/30/2011	294.8	3,423.1	3,128.3	8.6	3,451.8	90.6
6/30/2012	338.7	3,594.5	3,255.8	9.4	3,479.6	93.6
6/30/2013	412.2	3,521.1	3,108.9	11.7	3,480.0	89.3

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

Medical Insurance Plan – Schedule of Employer Contributions

Fiscal Year Ended	Annual Required Contribution (A)	Actual Employer Contribution (B)	Retiree Drug Subsidy Contribution (C)	Total Contribution (B) + (C)	Percentage of ARC Contribution [(B) + (C)]/(A)
6/30/2008	$ 395,282,164	$ 148,954,644	$ 11,911,565	$ 160,866,209	40.7%
6/30/2009	467,312,904	164,480,119	13,611,748	178,091,867	38.1
6/30/2010	457,054,117	158,765,496	14,614,285	173,379,781	37.9
6/30/2011	477,723,070	188,453,929	280,585	188,734,514	39.5
6/30/2012	470,217,067	177,450,206	297,639	177,747,845	37.8
6/30/2013	186,725,823	166,611,420		166,611,420	89.2

Life Insurance Fund – Schedule of Funding Progress

(Dollar amount in thousands)

Actuarial Valuation Date	Actuarial Value of Assets A	Actuarial Accrued Liabilities (AAL) B	Unfunded AAL (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll C	UAAL As a % of Covered Payroll [(B-A)/C]
6/30/2008	$ 77,658	$ 84,265	$ 6,607	92.2%	$ 3,190,332	0.21%
6/30/2009	84,703	90,334	5,631	93.8	3,253,077	0.17
6/30/2010	87,905	92,091	4,186	95.5	3,321,614	0.13
6/30/2011	88,527	88,088	(439)	100.5	3,451,756	(0.01)
6/30/2012	92,241	91,398	(843)	100.9	3,479,567	(0.02)
6/30/2013	94,863	94,325	(538)	100.6	3,480,066	(0.02)

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

Life Insurance Plan – Schedule of Employer Contributions

Fiscal Year Ended	Annual Required Contribution (ARC) (A)	Actual Employer Contribution (B)	Percentage of ARC Contributed (B) / (A)
6/30/2008	$ 1,914,199	$ 5,411,249	282.7%
6/30/2009	1,498,076	5,455,473	364.2
6/30/2010	1,992,969	1,966,826	98.7
6/30/2011	1,725,878	1,668,822	96.7
6/30/2012	1,732,831	1,684,711	97.2
6/30/2013	1,739,908	1,680,495	96.6

Required Supporting Schedules

Supporting Schedule 1
Schedule of Administrative Expenses
Year Ended June 30, 2013

Expense	Amount
Salaries	$ 6,670,002
Other Personnel Costs	760,113
Professional Services and Contracts	331,275
Utilities	93,986
Rentals	18,782
Maintenance	195,890
Postage & Related Services	420,965
Printing	74,389
Insurance	138,029
Miscellaneous Services	119,064
Telecommunications	33,068
Computer Services	108,199
Supplies	77,338
Depreciation	333,401
Travel	44,343
Dues & Subscriptions	45,113
Miscellaneous Commodities	16,730
Furniture, Fixtures, & Equipment not Capitalized	94,090
Compensated Absences	102,464
Total Administrative Expenses	**$ 9,677,241**

Supporting Schedule 2
Schedule of Professional Fees for Year Ended June 30, 2013

Professional	Nature of Service	Amount
Cavanaugh Macdonald Consulting	Actuarial Services	$ 207,604
Mountjoy Chilton Medley	Auditing Services	39,000
Farmers Bank	Bank Services	120
International Claim Specialist	Investigative Services	960
Groom Law Group	Attorney Services	2,000
Ice Miller	Attorney Services	40,934
Reinhart, Boerner VanDeuren	Attorney Services	216
Wyatt Tarrant and Combs	Attorney Services	32,273
Peritus	Communications	8,168
Total Professional Services and Contracts		**$ 331,275**

Note 9: Required Supplementary Information continued . . .

Supporting Schedule 3
Schedule of Contracted Investment Management Expenses and Miscellaneous Expenses
Year Ended June 30, 2013

	Pension	Medical	Total
Equity Managers			
Baillie Gifford	$ 2,152,311	$	$ 2,152,311
Baring Asset Management, Inc.	2,197,067		2,197,067
Black Rock	62,943	11,948	174,891
GE Asset Management	800,000		800,000
Todd-Veredus Asset Management LLC	1,271,143		1,271,143
UBS Global Asset Management	2,798,232		2,798,232
Wellington Management Company	2,827,337		2,827,337
Total Equity Managers	12,109,033	11,948	12,220,981
Fixed Income Managers			
Fort Washington Investment Advisors	160,533		160,533
Galliard Capital Management	287,976		287,976
Total Fixed Income Managers	448,509		448,509
Real Estate	3,956,528		3,956,528
Additional Categories	4,122,473	152,281	4,274,754
Alternative Investments	10,958,668	283,528	11,242,196
Custodian			
The Bank of New York Mellon	332,982	7,356	340,338
Consultant			
Hewitt Ennis Knupp, Inc.	358,850		358,850
Legal & Research			
Stoll, Keenon, Ogden, PLLC	888		888
Wolters Kluwer	3,952		3,952
Ice Miller	65,678		65,678
Bevis Longstreth	51,983		51,983
George Philip	33,269		33,269
Total Legal & Research	155,770		155,770
Other			
Subscription/Services	700,684	926	701,610
Total Contracted Investment Management Expenses	**$ 33,143,497**	**$ 556,039**	**$ 33,699,536**

Mountjoy
Chilton
Medley

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

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

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States the financial statements of the Teachers' Retirement System of the State of Kentucky, which comprise the statement of plan net position as of June 30, 2013, and the related statements of changes in plan net position for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 16, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Teachers' Retirement System of the State of Kentucky's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Teachers' Retirement System of the State of Kentucky's internal control. Accordingly, we do not express an opinion on the effectiveness of the Teachers' Retirement System of the State of Kentucky's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weakness or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Teachers' Retirement System of the State of Kentucky's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Teachers' Retirement System of the State of Kentucky's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the Teachers' Retirement System of the State of Kentucky's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

/s/ Mountjoy Chilton Medley LLP

Mountjoy Chilton Medley LLP

Lexington, KY
December 16, 2013

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