

MINUTES OF THE JOINT MEETING
OF THE BOARD OF TRUSTEES OF
THE KENTUCKY JUDICIAL FORM RETIREMENT SYSTEM,
THE INVESTMENT COMMITTEE FOR THE
KENTUCKY JUDICIAL RETIREMENT FUND,
AND THE INVESTMENT COMMITTEE FOR THE
KENTUCKY LEGISLATORS RETIREMENT FUND

January 21, 2022

The Board of Trustees of the Kentucky Judicial Form Retirement System (JFRS), the Investment Committee for the Kentucky Judicial Retirement Plan (JRP), and the Investment Committee for the Kentucky Legislators Retirement Plan (LRP), convened at the Administrative Office of the Courts, 1001 Vandalay Drive, Frankfort, Kentucky 40601 on Friday, January 21, 2022, at 10:00 a.m. All Board members were present, with the exception of Senator Joe Bowen, who participated virtually via a Microsoft Team Meeting.

JFRS staff present included Bo Cracraft, Executive Director, and Rebecca Stephens, Retirement Programs Administrator. Guests attending the meeting virtually via Microsoft Teams video-conferencing included Don Asfahl, Andy Means, and John Watkins of Baird Trust Company, Kevin Hart and Kevin Hicks of Milliman, Inc, and Alan Pauw of McBrayer, PLLC.

Chairman Grise called the meeting to order at 10:01 a.m.

The trustees considered the adoption of the previously distributed *Minutes* from the October 22, 2021 meeting. Upon motion by Judge Douglas George, seconded by Justice Daniel Venters, the Board unanimously approved the *Minutes* of the October 22, 2021 meeting.

The next order of business was a review of the quarterly Lexington Investments LLC report. Chairman Grise recognized Mr. Cracraft, who informed the Board that Mr. Stan Kerrick would not be joining the quarterly meeting. Instead, Mr. Cracraft had prepared a staff report to highlight a Mr. Kerrick's *Report of the Kentucky Judicial & Legislators Retirement Funds* as of December 31, 2021, which was included in the meeting materials.

Mr. Cracraft began by pointing out Mr. Kerrick's compliance statement, which noted both Plans were within their prescribed asset allocation guidelines. He also highlighted that neither plan currently had individual equity positions that exceed the 8% maximum weighting. Next, Mr. Cracraft quickly drew attention to performance results, where both portfolios saw strong positive gains during the second quarter of the fiscal year. Longer-term both continued to provide above benchmark returns and had exceed the actuarially assumed rate of return. Lastly, Mr. Cracraft reviewed cash transaction reports, which included the sale of Microsoft, which was an equity holding that had slightly exceed the portfolio's max holding guideline during the prior quarter. He also informed the board that since the close of the quarter, during the first week of January, the team at Baird had executed a rebalancing trade and had drew down the overall equity allocation.

Chairman Grise welcomed members of Baird Trust Company (formerly known as Hilliard Lyons Trust Company), who joined the meeting virtually via Microsoft Teams at 10:13

a.m. Mr. Cracraft had previously distributed copies of Hilliard Lyons' *Investment Review for Kentucky Judicial Retirement Fund and Kentucky Legislators Retirement Fund* dated January 21, 2022

Mr. Andy Means began the quarterly review with a few comments regarding Baird's most recent quarterly Market Commentary, titled "The Main Thing," which tried to reconcile how investors had experienced a historically strong stock market in the face of two pandemic-laden years. First, Mr. Means pointed to the massive fiscal and monetary policy response to the pandemic, which flushed liquidity into markets and served to life asset values almost across the board. However, just as important, Mr. Means discussed the amazing growth of technological innovation, which has resulted in the United States becoming the undisputed leader of the digital revolution that is changing many aspects of how we work, communicate, and play. The massive moves to work-from-home and hybrid work environments have boosted the growth rate of the domestic technology industry and made the U.S. stock market the envy of the world.

Moving forward, Mr. Means reiterated Baird would focus on wading through the unknowable future, avoiding the many distractions that exist or will occur, and investing in productive assets the team believes will provide stable streams of income in all market cycles. He noted the past two years have served as an emphatic reminder that investors do not know the future, so the investment team was going to continue focusing their time on things that are knowable. He also pointed to the numerous distractions that had occurred and the need for investors to stay focused and disciplined in a rapidly changing and high speed markets. Lastly, Mr. Mean emphasized the team would remain focused on the main thing, which for them is finding high quality companies, with strong management teams, and not investing in areas outside their circle of competence. One such area is the broad and highly publicized area of nonproductive assets, which produce little to no cash flow and thus very limited downside protection.

Mr. Asfahl reviewed current asset allocation, annual estimated income, and the current yield on the JRP legacy portfolio. He discussed the fixed income portfolio and schedule of maturities. Mr. Means reviewed a snapshot of the portfolio, which included relative sector weightings, top performers and largest holdings. He reiterated the teams' goal was to materially outperform the index, which meant sector allocations would often look quite a bit different from the index. He emphasized sector weighting was not the result of any macro or top-down, decisions, but rather completely driven by the underlying stocks. He pointed out the portfolio was currently overweigh to discretionary, financials, real estate and industrials, versus underweights to technology and health care.

Next, Mr. John Watkins reviewed a couple of trades that had occurring during the quarter. After consecutive quarters with no turnover, the team made two small changes to the portfolio in November. First, after holding the stock for almost a decade, the team decided to exit their position in Northern Trust. Mr. Watkins noted the stock had been a strong performer for the portfolio historically, but an overall change in fundamentals had served as a catalyst to change their opinion on the stock. In exchange, the team added to an existing position in General Electric, which had been a very strong performer recently. Secondly, the team also trimmed their position in Microsoft, which had reached the 8% maximum position. Mr. Watkins stated it was the second time the stock was trimmed during the year and that proceeds were added to an existing position in Johnson & Johnson. Lastly, Mr. Watkins also informed the Board that the

equity portfolio had also be fully rebalanced during the first week of January to help reduce overall equity exposure and bring the portfolio back closer to the 70% target. A portion of the cash was withdrawn by JFRS staff for benefit payments, while the rest would be invested in fixed income.

Mr. Asfahl concluded the presentation with a short review of the fixed income portion of the portfolios, a summary of risk statistics, as well as trailing period performance of the portfolios. He advised that the portfolios were well-positioned, continued to produce strong risk adjusted results, and had outperformed the blended index over each measured period.

In response to a question from Mr. Cracraft regarding if a change in the assumed rate of return would result in Baird proposing revised asset allocation changes, both Mr. Asfahl and Mr. Means expressed confidence the team would not suggest major changes to the portfolio mix of equity and fixed. First, Mr. Asfahl referenced current interest rates and the headwind facing corporate bonds. Mr. Means added that the portfolio's current equity holdings also had a very strong income component and many were increasing dividends.

Mr. Steven LeLaurin and Mr. Ben Allison also pointed out that a change in the assumed rate of return would not necessary require a change in the portfolio's asset allocation and changing the assumption would have an impact in other areas, such as the calculation of each plans' accrued liability of future benefits.

In response to a question from Senator Bowen regarding dividends and if the Baird team targeted companies who provided, Mr. Means responded that it was not necessarily a target or requirement but generally a result of the companies the team chooses to hold. He noted the team looks for companies that generate consistent free cash flow and management teams that utilize that cash flow successfully. While in many cases this has led to consistent and growing dividends, there are companies that will instead reinvest that cash flow and grow the business.

Lastly, Mr. Asfahl quickly reviewed allocation, returns, and holdings for the smaller Cash Balance portfolios. He referenced the Board recent decision to diversify the portfolios and pointed to the most recent quarterly performance as evidence of how the tracking error between the two portfolios had really tightened.

Mr. Mean's and Mr. Watkins left the meeting at 10:55 a.m., while Mr. Asfahl remained online to participate in the next agenda item.

Chairman Grise recognized Mr. Cracraft to report on the next item, a review of proposed changes to the JFRS Investment Policy Statement.

Mr. Cracraft began by referencing an *Investment Policy – January 2022 Update* that was included in the Board materials. He reminded the trustees of a discussion during the October meeting regarding some needed updates and revisions to the policies. Since October, the committee chairs, along with Mr. Allison have put together a revised policy.

Mr. Cracraft walked through each of the individual changes, which fell into one of three primary categories. First, several changes were made to incorporate the Board's recent decision to diversify the cash balance portfolios to add active management and better mirror the

investment strategy employed in the larger legacy assets. Secondly, staff had requested a handful of technical changes to better align with current day-to-day administration and monitoring of the portfolios. Third, after a review of the proposed changes, the Baird investment team had requested a few additional changes.

Following a healthy discussion, Mr. Stephen LeLaurin made a motion on behalf of the Investment Committee for the Judicial Retirement Fund, which was seconded by Judge Douglas George, and Senator Joe Bowen made a motion on behalf of the Investment Committee for the Legislative Retirement Fund, which was seconded by Representative Brad Montell, to adopt the revised Investment Policy Statements. The motions passed both committees unanimously.

Mr. Asfahl left the meeting at 11:35 a.m.

Chairman Grise recognized Mr. Cracraft, who reported on several administrative matters. The trustees discussed the items and took action when noted.

(A) Public Pension Oversight Board (PPOB). Mr. Cracraft gave a summary of PPOB meetings since the October JFRS Board meeting.

November 22, 2021. Each state-administered retirement system presented annual valuation results, along with a review of fiscal year end performance and cash flow. JFRS also was given an opportunity to present a propose 2022 Housekeeping bill for the agency.

December 20, 2021. JFRS was not on the agenda, but the Board did approve their annual recommendations, which included the JFRS housekeeping legislative proposal. In addition, the oversight Board approved issuing a RFP to hire an actuarial firm to conduct a Level 1 (full scope) actuarial audit of all three pension administrators.

January 24, 2022. Meeting was scheduled for the following Monday. JFRS was no on the agenda, which only included an annual investment review by LRC staff.

(C) 2022 General Session. Mr. Cracraft referenced the *2022 Regular Session – Legislative Update* memo from staff included in the Board materials. He discussed the first couple of weeks of the Regular Session and highlighted a few retirement related proposals. Most notably, he informed the board that the JFRS housekeeping bill was filed as Senate Bill 32 and assigned to the Senate State and Local Government Committee. He expressed some hope that the committee would consider the bill in the coming week and with some favor, it could be voted on by the full Senate by early February. In addition, he reviewed the proposed Legislative and Judicial Branch budget bills, which had both been passed by the House of Representatives.

(F) Fiscal Year 2021 APA Audit Reports. Mr. Cracraft informed the Board that copies of the APA Audit Reports were included in the Board materials. He reminded the Board that the reports were also emailed to each Trustee in November upon receipt.

(G) Financial Disclosure Statements. Mr. Cracraft requested that each trustee complete a Financial Disclosure Report for calendar year 2021 on or before March 31, 2022 in order to comply with the annual mandated disclosure requirement. A copy of the disclosure had been emailed to each trustee and he provided hard copies to those members in attendance.

The meeting recessed for lunch at 12:00 p.m.

The meeting reconvened at 12:15 p.m. Mr. Cracraft continued his reports on administrative matters. The trustees discussed the items and took action when noted.

(C) 2022-2023 Personal Service Contracts.

1. **Investment Management.** The May 10, 2019 Personal Service Contract with Hilliard Lyons Trust Company contained an option to extend the contract for two additional one-year periods beginning on July 1, 2020 under the same terms and conditions at a fee of eight (8) basis points. In June of 2020 and 2021, the contract was extended for additional 1-year periods. With no remaining extensions, the current investment management contract is set to expire on June 30, 2022.

The investment counseling and management services for the assets of the two retirement plans were reviewed and discussed. Mr. Stephen LeLaurin made a motion on behalf of the Investment Committee for the Judicial Retirement Fund, which was seconded by Justice Daniel Venters, and Senator Joe Bowen made a motion on behalf of the Investment Committee for the Legislative Retirement Fund, which was seconded by Representative Scott Brinkman, to extend an offer to Baird Trust Company for management and counsel services for Judicial Form Retirement System's plan assets for the period of July 1, 2022 through June 30, 2024 under the same terms and conditions.

2. **Audit Services.** An RFP was issued in early 2018 and resulted in JFRS contracting with MCM CPAs & Advisors for auditing services for the period July 1, 2018 through June 30, 2019, at the annual fee of \$17,750.00. The contract provided for two additional one-year extensions, which were executed in June of 2019 and 2020.

During the April 2021 meeting, the Board approved engaging MCM for one additional year for the sole purpose of compiling fiscal year 2021 financial statements and assisting staff with the upcoming APA audit with an expectation that JFRS would then issue a full RFP in early 2022.

After a short discussion, Representative Brad Montell made a motion, seconded by Mr. Ben Allison, to issue a RFP for JFRS audit services in accordance with the Commonwealth's Model Procurement Code. The motion passed unanimously.

3. **Actuarial Consulting.** Both the Investment Committee for the Judicial and Legislators Retirement Funds entered into a contract with Findley, Inc. on June 26, 2018 for actuarial services which expired on June 30, 2020. The contract provided for two additional two-year extensions, with an initial extension agreed upon in May 2020.

Mr. Cracraft noted that both committees agreed to extend the original contract and on May 21, 2020, a two-year extension was agreed upon which will not expire until June 30, 2022.

The actuarial services for Judicial Form Retirement System were reviewed and discussed. Mr. Stephen LeLaurin made a motion on behalf of the Investment Committee for the Judicial Retirement Fund, which was seconded by Justice Daniel Venters, and Senator Joe Bowen made a motion on behalf of the Investment Committee for the Legislative Retirement Fund, which was seconded by Representative Scott Brink, to offer USI, Inc. (formerly known as Findley) a 2-year extension under the terms and conditions as outlined in a personal services contract extension dated June 26, 2018. Both Committees unanimously adopted.

4. **Custodian.** State Street remains the custodian of the Funds. The Commonwealth of Kentucky and State Street are the parties to the current contract, which was last extended for a 2-year period in 2019 and scheduled to expire June 30, 2021. The 2019 extension included services to JFRS as a named agency of the Commonwealth.

Mr. Cracraft noted the current extension was set to expire effective June 30, 2022. He advised that he was in process of trying to determine what the Commonwealth's future plans were and if JFRS could remain a named agency. Following discussion, it was the consensus of the trustees that JFRS continue to participate in the Commonwealth's custodian contract with State Street.

(D) JFRS Pension Administrative Software RFP. Mr. Cracraft referenced the *Pension Administration Software Recommendation* memo that was included in the Board materials.

Mr. Cracraft informed the Board the evaluation committee was excited to recommend the Board hire Milliman, Inc. to provide a new pension administrative system for JFRS. Member of the Milliman team were planning to join the meeting to provide a short demonstration of the firm's Milliman Actuarial Retirement Calculator ("MARC") software.

Mr. Cracraft quickly reviewed the process following during the process. He noted that JFRS received three proposals in response to the RFP. After a review of the written proposals, the Committee designated two firms as finalists for further evaluation. Mr. Cracraft noted the third response did meet the minimum qualifications of the RFP, but the proposed solution was a more complex and customizable approach that came at a cost that did not fit the project's expected budget. Next, the two finalists, Milliman Inc. and PensionSoft, provided virtual demonstrations of their software systems and the Committee met and interviewed key project team members. Following the interviews and software demonstrations, each member of the Committee scored both finalists independently based on criteria that included qualification, experience, implementation, functionality, and cost.

Mr. Cracraft stated the committee was impressed with both finalists and believed that either could meet the goals of the project. However, when each evaluator scored the two finalists, the Milliman MARC platform ranked higher than PensionSoft's DB Precision tool. He pointed to a few differentiating factors. First, the MARC solution was completely cloud-based, while the DB Precision solution offered by PensionSoft was a combination of both on-site and cloud-based storage. Given JFRS's small size and limited IT and security capabilities, the Committee favored the cloud-based option and experienced team that would service and maintain the MARC

platform. Secondly, while both platforms were out-of-the-box tools, the MARC system offers more customization and provides a testing environment that made it more adaptable to changes that could occur in the future. Given a history of legislative changes and plans that offer two very different tiers of benefits, the Committee believed Milliman provided a better long-term solution. Third, the Committee rated Milliman's team and experience providing PAS systems slightly higher than PensionSoft. Milliman has a significantly larger and more robust team, but importantly the key members assigned to JFRS have each been with the firm a minimum of 15 years and have experience working with pension plans similar in size to JFRS. Lastly, the user interface of the MARC system felt more organized and intuitive to staff, and the Committee rated the online member self-service portal higher between the two finalists.

In closing, Mr. Cracraft discussed the proposed cost for implementation and annual licensing fees. He noted the Milliman MARC platform did come as a slightly higher cost. The proposed annual licensing fee, while approximately 10% higher than PensionSoft, included maintenance and service on the fully cloud-based system. Furthermore, the Committee believed added features such as a testing environment merited the slightly higher annual cost. On the implementation side, Milliman's proposed maximum cost was also higher, but the Committee did not believe a marginally higher one-time cost outweighed the long-term improvements that would result from a system the entire Committee believed was the best solution for JFRS.

Next, Chairman Grise welcomed Kevin Hart and Kevin Hicks, from Milliman, Inc., who joined the meeting virtually via Microsoft Teams at 12:35 p.m. Mr. Hart provided a short demonstration of the MARC software platform, specifically focusing much of his time on the member self-service portal, retirement estimate process, document library and ability for member to share documents with JFRS in a secure and simple manner. Mr. Hart also provided a brief review of the administrative tool that staff would utilize on a daily basis.

In response to a question from Mr. Cracraft regarding the proposed timeline of implementation, Mr. Hart responded that most projects of this size take approximately nine months and do include a lot of calls, meetings, document reviews, and data verification. The Milliman team, which will be led by Mr. Hicks, will create a timeline and will work with JFRS staff on a daily basis.

In response to questions from Justice Venters and Judge Grise regarding security and access to the underlying member data, Mr. Hart emphasized that all data would be held securely and that Milliman does not share or use the underlying data for other purposes. Mr. Hart reassured the trustees that JFRS would have access to all member data, even in the event a relationship with Milliman was ended.

Mr. Hart and Mr. Hicks left the meeting at 1:10 p.m.

After a healthy discussion amongst the trustees regarding costs, expected improvements in benefit administration, and the opportunity to modernize the plan going forward, Judge Douglas George made a motion, seconded by Mr. Ben Allison, to engage Milliman, Inc. for the purpose of providing a Pension Administrative System pending successful contract negotiations and a legal review by JFRS' third-party legal counsel.

(E) Non-Judicial or Non-Legislative Participation Date Discussion. Mr. Cracraft referenced the *Participation Date for Non-Judicial and Non-Legislative Service* memo that was included in the Board materials. He quickly provided some background and what led staff to request a legal opinion from Mr. Alan Pauw, who was also preparing to join the meeting to discuss and review his letter.

Mr. Alan Pauw, from McBrayer, PLLC joined the meeting virtually via Microsoft Teams at 1:30 p.m. Mr. Pauw quickly provided a review of his memo and the statutory references he believed applied to the question of participation, reciprocity, and eligibility of JRP or LRP members who also had prior service at another state-administered pension plan.

In response to a question from Judge Douglas George regarding the agency's current interpretation and administration of such situations, Mr. Pauw responded that he did believe staff was administering in a manner that was consistent and could be supported by the statutory language he reviewed.

There was a discussion amongst the trustees regarding Mr. Pauw's letter and the agency's current policy of administrating situations. Following the discussion, it was the consensus of the trustees that JFRS would continue to follow current policy when counseling new and prospective members.

The next agenda item was Executive Session. Upon motion by Justice Daniel Venters, seconded by Representative Brad Montell, the Board unanimously agreed to go into Executive Session for the purpose of discussing personnel and confidential member information of an employee. The motion passed unanimously.

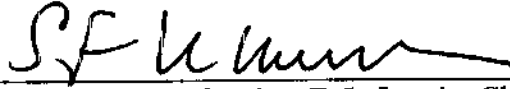
Upon motion by Judge Douglas George, seconded by Mr. Stephen LeLaurin, the Board unanimously agreed to come out of Executive Session. No action was taken in Executive Session.

Upon motion by Mr. Steven LeLaurin, seconded by Judge Douglas George, the Board unanimously authorized a raise in the salary of Carlos "Bo" Cracraft as the Executive Director of JFRS effective 02/01/2022 to an annual salary of \$130,000 per year, paid semi-monthly on the 15th and the 30th of each month.

There being no further business, the meeting adjourned at 2:44 p.m.



Judge John R. Grise, Chairman
Judicial Form Retirement System Board of Trustees



Stephen F. LeLaurin, Chairman
Judicial Retirement Fund Investment Committee

Joe R. Bowen, Chairman*
Legislators Retirement Fund Investment Committee

** deceased March 8, 2022*



Bo Cracraft, Executive Director