

STATE OF KANSAS
PUBLIC EMPLOYEES DEFERRED COMPENSATION PLAN
AND
AND KPERS SUPPLEMENTAL DEFINED CONTRIBUTION PLAN

Statement of Investment Policy

November 2016

STATE OF KANSAS DEFERRED COMPENSATION PLAN & KPERs SUPPLEMENTAL DEFINED CONTRIBUTION PLAN

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The State of Kansas (the State) on behalf of the State of Kansas Deferred Compensation Plan (KPERS 457 Plan) and the KPERS Supplemental Defined Contribution Plan (KPERS 401(a) plan), together referred to as “the Plans,” through the KPERS Board of Trustees (Board), hereby adopts this Statement of Investment Policy (Statement) for the Plans.

SECTION 1: Objectives of the Plans

The Plans are long-term retirement savings vehicles and are intended as a source of retirement income for eligible participants. The investment funds available from the Plans cover a broad range of investment risk and rewards appropriate for these kinds of retirement savings programs. Participants bear the risk and reap the rewards of investment returns that result from the investment funds they select.

This Statement of Investment Policy serves the following purposes:

- To ensure that a broad range of investment funds are offered to the Plans’ participants;
- To establish an investment program that will allow the Plans’ participants the opportunity to structure an investment strategy that meets their individual return objectives and risk tolerances;
- To define the investment categories that may be offered by the Plans;
- To establish investment objectives and guidelines for each investment category offered within the Plans;
- To establish benchmarks and performance standards for each investment category and guidelines for evaluating each fund’s performance against appropriate benchmarks and standards;
- To establish criteria for selection of investment funds;
- To establish objectives and guidelines for determining the administrative assessment rate and process;
- To establish a procedure for reporting and monitoring of the various investment funds;
- To define the procedures for investment fund evaluation and formal investment fund review; and
- To set guidelines and procedures for replacing an investment fund that, in the Board’s opinion, does not, or will not, fulfill the Plans’ objectives or performance standards for which it was selected and replace the fund with an appropriate substitute.

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SECTION 2: Investment Categories Objectives & Benchmarks

The Board has chosen to offer investment funds in up to 15 investment categories, plus a series of Target Date Funds, as further described below:

Category
Stable Value
Core Fixed Income
Balanced
Large Cap Value Equity
Large Cap Blend Equity (passive)
Large Cap Blend Equity (active)
Large Cap Growth Equity
Mid Cap Value Equity
Mid Cap Blend Equity (passive)
Mid Cap Growth Equity
Small Cap Value Equity
Small Cap Blend Equity (passive)
Small Cap Growth Equity
International Equity
Global Equity
Series of Target Date Funds

Each investment fund offered under the Plans shall:

- Operate in full accordance with its current published prospectus or “fact sheet”; and
- Have its performance results measured against the applicable performance standards described herein for that investment category.

If the Board determines an investment fund no longer meets the performance criteria, it may replace that fund with a suitable alternative pursuant to the investment fund evaluation procedure outlined herein. From time-to-time, the Board, in its discretion, may add investment funds/categories to the current core funds. At such time, the Statement of Investment Policy will be modified to include those changes.

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The Board seeks to offer best-in-class investment fund(s) in the investment asset categories listed above and as further described in the remainder of this section.

Stable Value

Objective

The objective of this category is to preserve principal and provide a stable, competitive rate of return. An investment fund in this category invests in fixed income instruments, including those of the U.S. Government and its agencies; other developed nations; corporations, and mortgage and asset-backed securities.

Performance Standards

The performance of the Stable Value Fund will be evaluated primarily with regard to the crediting rate received by participants. In order to assess whether the fund is providing a competitive declared net crediting rate, the crediting rate will be compared against the E-vestment Alliance Stable Value Universe. A supplemental performance standard is for the underlying portfolio to outperform the Barclays Intermediate Aggregate Index over a full market cycle. Use of the index does not imply that performance of the portfolio will replicate the index.

The weighted average credit quality of the portfolio is to be no less than AA- at any time. The portfolio will have a maximum effective duration of 4.0 years, regardless of the duration of the benchmark. Other investment guidelines are specified in the investment management agreement with Empower.

Core Fixed Income

Objective

The objective of this investment category is to provide total return consistent with preservation of capital by investing in fixed income instruments, including corporate, government and mortgage-backed securities. Investment returns are expected to be derived primarily from current income.

Performance Benchmark and Peer Group: Barclays Capital Aggregate Bond and the core fixed income fund universe.

Balanced

Objective

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The objective of this investment category is to invest in stocks, bonds, and cash to provide capital appreciation and income with less volatility than an all-stock fund. Investment returns are expected to be derived from a combination of capital appreciation and dividend and interest income.

Performance Benchmark and Peer Group: 60% S&P 500 Index and 40% Barclays Capital Aggregate Bond Index composite and the balanced fund universe.

Large Cap Value Equity

Objective

The objective of this investment category is to invest primarily in the common stock of large capitalization domestic companies considered by the fund manager to be undervalued relative to the market. Investment returns should primarily be derived from capital appreciation and, to a lesser degree, dividend income.

Performance Benchmark and Peer Group: Russell 1000 Value Index and the large cap value equity fund universe.

Large Cap Blend Equity (passive)

Objective

The objective of this investment category is to approximate the performance of the Standard & Poor's 500 Index by investing in common stock of the large capitalization domestic companies comprising the Index. The S&P 500 Index is an equity composite of the 500 largest companies in the United States based on market capitalization. Investment returns are expected to be derived primarily from capital appreciation and, to a lesser degree, dividend income.

Performance Benchmark and Peer Group (Secondary Consideration): S&P 500 Index and the large cap blend equity fund universe.

Large Cap Blend Equity (active)

Objective

The objective of this investment category is to invest primarily in the common stock of large capitalization domestic companies considered by the fund manager to be undervalued relative to the market or to have above-average potential for capital appreciation. Investment returns are expected to be derived primarily from capital appreciation and, to a lesser degree, dividend income.

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Performance Benchmark and Peer Group: S&P 500 Index and the large cap blend equity fund universe.

Large Cap Growth Equity

Objective

The objective of this investment category is to invest primarily in the common stock of large capitalization domestic companies considered by the fund manager to have above average potential for capital appreciation. Investment returns are expected to be derived primarily from capital appreciation.

Performance Benchmark and Peer Group: Russell 1000 Growth Index and the large cap growth equity fund universe.

Mid Cap Value Equity

Objective

The objective of this investment category is to invest primarily in the common stocks of medium-sized companies considered by the fund manager to be undervalued relative to the market. Investment returns should be derived primarily from capital appreciation and, to a lesser degree, dividend income.

Performance Benchmark and Peer Group: Russell Mid Cap Value Index and the mid cap value equity fund universe.

Mid Cap Blend Equity (passive)

Objective

The objective of this investment category is to approximate the performance of the Russell Mid Cap Index or the MSCI Mid Cap 450 Index by investing in the common stocks of medium-sized companies comprising the Index. Investment returns should be derived primarily from capital appreciation and, to a lesser extent, dividend income.

Performance Benchmark and Peer Group (Secondary Consideration): Russell Mid Cap Index or the MSCI Mid Cap 450 Index and the mid cap equity fund universe.

Mid Cap Growth Equity

Objective

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The objective of this investment category is to invest primarily in the common stocks of medium-sized companies considered by the fund manager to have above average potential for capital appreciation. Investment returns should be derived primarily from capital appreciation.

Performance Benchmark and Peer Group: Russell Mid Cap Growth Index and the mid cap growth equity fund universe.

Small Cap Value Equity

Objective

The objective of this investment category is to invest primarily in the common stocks of small-sized companies considered by the fund manager to be undervalued relative to the market. Investment returns should be derived primarily from capital appreciation and, to a lesser degree, dividend income.

Performance Benchmark and Peer Group: Russell 2000 Value Index and the small cap value equity fund universe.

Small Cap Blend Equity (passive)

Objective

The objective of this investment category is to approximate the performance of the Russell 2000 Index or the MSCI Small Cap 1750 by investing primarily in the common stocks of small-sized companies comprising the Index. Investment returns are expected to be derived primarily from capital appreciation and, to a lesser degree, dividend income.

Performance Benchmark and Peer Group (Secondary Consideration): Russell 2000 Index or the MSCI Small Cap 1750 and the small cap equity fund universe.

Small Cap Growth Equity

Objective

The objective of this investment category is to invest primarily in the common stocks of small-sized companies considered by the fund manager to have above average potential for capital appreciation. Investment returns should be derived primarily from capital appreciation.

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Performance Benchmark and Peer Group: Russell 2000 Growth Index and the small cap growth equity fund universe.

International Equity

Objective

The objective of this investment category is to invest primarily in the common stock of companies located outside the United States. Investment returns are expected to be derived primarily from capital appreciation.

Performance Benchmark and Peer Group: the MSCI All-Country World ex-US Index (net dividends) and the international equity fund universe.

Global Equity

Objective

The objective of this investment category is to invest primarily in the common stock of companies located throughout the world, including the United States. Investment returns are expected to be derived primarily from capital appreciation.

Performance Benchmark and Peer Group: MSCI World Index (net dividends) and the global equity fund universe.

Target Date

Objective

The objective of this investment category is to invest in equity, fixed income and/or money market instruments using asset allocations targeting a stated investment time horizon. The funds have a targeted “maturity date” that should coincide with the Participant’s investment horizon. As the “maturity date” is approached, the asset allocation shifts from a heavier equity allocation, to a balanced portfolio, to primarily fixed income. Investment returns are expected to be derived from current income and/or capital appreciation, based on the target allocation of the particular fund.

Performance Benchmark: An index-based, composite index based on the broad asset allocation of the underlying portfolios.

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Section 3: Investment Fund Selection

If the Board elects to add or replace an investment fund in one of the asset classes outlined in this policy, searches for investment funds within that asset class will be among funds that have demonstrated a successful track record. In addition, it is expected that actively managed investment funds will have above median performance for a trailing period of at least three years or longer.

The Committee will select funds that are generally well diversified. Funds with less than 60 securities and more than 35% of the portfolio held in the top 10 securities will be avoided unless the Committee makes a specific exception.

In selecting an investment fund, a due diligence process is followed that analyzes the investment fund in terms of certain attributes, including but not limited to:

- 1) Investment performance track record.
- 2) Investment management expense. Expense ratios below the median for the asset class are preferred but not required.
- 3) Length of time since inception. Investment funds must have a minimum of a three-year track record, unless it is an index-based fund.
- 4) Size of fund. The investment fund must have at least \$100 million in fund assets prior to the investment by the Plans.
- 5) Investment risk characteristics as measured by the standard deviation of returns and beta.
- 6) Risk adjusted returns as measured by Sharpe ratio and alpha.
- 7) Alignment of investment fund style with investment mandate.
- 8) Tenure of investment management team.
- 9) Compatibility with the Plan's record keeper platform trading requirements.

Target Date Fund Selection. When the Committee is evaluating funds for the target date asset class, the Committee will first focus on the risk profile, equity-to-fixed income ratios over time, and asset allocation (the 'glide path' of the entire target date suite). The Committee will assess the reasonableness of the risk profile. Consideration will also be given to investment costs of the Target Date funds. In addition, fund performance will be evaluated against an index benchmark reasonably based on the broad asset allocation of the underlying portfolios.

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SECTION 4: Plan-Level Reporting and Monitoring Procedures

The Board, through its Deferred Compensation Committee and with assistance from the Investment Consultant, will review the Plans periodically, but no less than annually. The review will include the following:

- Current trends and developments in the capital markets and investment management community (market review);
- The current level of diversification provided by the investment categories and funds offered by the Plans under the investment fund line-up (review of the correlation between investment categories and funds);
- Changes in the investment management staff related to each investment fund (organizational review);
- The continued consistency between the stated investment guidelines for each investment fund and the Plans' policies (review of the guidelines, along with holdings and characteristics of each investment fund, and style drift analysis);
- As outlined in Section 5 below, the compliance of each investment fund's risk and return characteristics with the expectations stated herein (investment fund performance evaluation); and
- Fees charged by each investment fund compared to industry benchmarks and other investment fund fees.

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SECTION 5: Investment Fund Performance Evaluation

The Committee will review the performance of investment funds to determine if they are performing in line with the established benchmarks (peer group and index performance comparisons). These reviews will generally be conducted on a quarterly basis. Performance benchmarks and the relevant peer group will be established and set out in this investment policy for each asset class at the time the class is included in the Plans.

The performance review will include measuring the investment fund's return against stated benchmarks and peer groups. The following general criteria will be used in the evaluation:

1) **Quantitative Criteria:**

- a) **Actively Managed Investment Funds.** Investment funds employing active management are expected to exceed the return of the benchmark for that asset class and to have investment return rankings above the median (50th percentile) of the relevant peer group for the trailing three year, five-year and/or longer time periods. Fund performance for trailing periods from 7 to 10 years will be weighted highest, followed by performance over periods of three to five years. In all evaluations, the longer time periods will be weighted more heavily than the shorter time periods. Risk, as measured by the standard deviation of quarterly returns, shall be consistent with that of the benchmark and peer group for that asset class. Returns used for these performance reviews are to be net of fees. Representative benchmarks and peer groups are identified for each asset class in Section 2 of this policy.
- b) **Passive Investment Strategies.** Passive investment funds are expected to track the investment return of the index strategy that the investment fund is designed to replicate, less management fees, with marginal tracking error. Typically rolling three- and five-year periods will be evaluated. It is also expected that the risk of each investment fund, as defined by standard deviation of returns, be commensurate with the appropriate market index. The index benchmarks and peer groups are identified for each asset class in Section 2 of this policy.

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c) Target Date Funds. Investment performance will be evaluated first against an index-based benchmark based on the broad asset allocation of the underlying portfolios, as described in Section 2. The composite indices for all the funds will consistently change allocation by gradually shifting its allocation towards money market and fixed income instruments as the fund matures.

2) **Time Periods:**

The Committee acknowledges that fluctuating rates of return characterize the securities markets, particularly during short-term time periods. Recognizing that short-term fluctuations may cause variations in an investment fund's performance, the Committee intends to employ investment funds with long-term investment strategies and will evaluate investment fund performance from a long-term perspective. For example, performance over three-, five-, and 10-year periods will be weighted more heavily than performance over shorter time periods, such as one-year or less.

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SECTION 6: Formal Review and Evaluation of Investment Funds

The Board, in its discretion, may conduct an informal review and evaluation of an investment fund at any time. A formal procedure for heightened due diligence of the Plans' investment funds follows.

Investment Fund Watch Status

All investment funds are expected to perform in line with the quantitative and qualitative criteria outlined above. The Committee recognizes the long-term nature of retirement investing and the variability of market returns. Periodic underperformance or variation from the criteria outlined above will not necessitate the termination of an investment fund. Underperformance will trigger review and consideration by the Committee of factors contributing to underperformance and possible courses of action that the Committee may take. The Committee will maintain a "watch list" consisting of any investment funds that it has determined will be subject to this heightened review and monitoring due to underperformance.

Automatic Watch Rule

At a minimum, the Committee will place an actively managed investment fund on the watch list if, for two consecutive quarters, the investment fund's performance is below the 75th percentile of its peer group over both the three- and five-year trailing periods. This is a minimum requirement that does not preclude placing a fund on the watch list for underperformance when the Committee deems it prudent to do so under other circumstances.

General Watch Considerations

The Committee may place any investment fund on the watch list due to one or more other factors, including the following:

- 1) Significant increase in management fees or expense ratios;
- 2) Investment risk characteristics, as measured by standard deviation and beta;
- 3) Risk adjusted returns, as measured by Sharpe ratio or alpha;
- 4) Turnover or imminent turnover in the management team of the investment fund;
- 5) Deviation from style and/or market cap range for which the investment fund was selected. As part of its ongoing evaluation of the stable value fund, the Board will

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monitor any reports of violations of the weighted average credit quality, average duration, and investment allocation standards, as well as the steps taken by the investment manager to correct those violations;

- 6) Significant organizational change, changes in ownership, mergers, etc.;
- 7) The investment fund has violated an SEC rule or regulation;
- 8) The fund has experienced other changes or problems in its procedures, operations, investing, or reporting which, in the Board's view, has or could detract from the objectives of the Plans; and
- 9) Other factors that the Committee may determine are important for consideration.

Termination of Watch Status

An investment fund may remain on watch status until the Committee decides to take further action. Committee actions include, but are not limited to, the following:

- 1) Remove the investment fund from watch status;
- 2) Continue the investment fund in watch status;
- 3) "Freeze" or close the investment fund to new deferrals, rollovers, or transfers; or
- 4) Terminate the investment fund and reallocate fund assets to an alternate fund or replacement fund by Committee direction.

When the Board freezes or terminates a fund, all participants must be promptly notified of the Board's action and of alternatives available through the Plans. An investment fund that was placed on the watch list due to underperformance may be removed from watch status if performance exceeds the median for both the trailing three and five year periods for two consecutive quarters.

Investment Fund Termination

The Committee will endeavor to use its best judgment and information available to act in a prudent manner on behalf of the Plans and the participants. The Committee reserves the right to terminate any Investment Fund at any time for any reason when it determines such termination is in the best interests of the Plans and the participants and beneficiaries.

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SECTION 7: General Provisions

State of Kansas Responsibilities

As set forth in K.S.A. 74-49b10 and 74-49b15, the State of Kansas is not responsible for any loss incurred by a participant under the Kansas Public Employees Deferred Compensation Plan or the KPERS Supplemental Defined Contribution Plan (KPERS 401(a) plan).

Responsibilities of the Participants

The participants in the Plans are responsible for making ALL investment decisions relating to their account balances. Information will be made available so participants may better understand their investment choices. It will be the participants' responsibility to examine this information and to seek out additional information if necessary.

Administrative Policies & Objectives

The Plans will be administered and records will be maintained in such a way as to provide daily transactions and access to account information.

Design and Administration of the Plans

The Plans are governed by the rules and requirements specified in the Plan Document of the respective Plan, as well as any applicable federal and state laws or regulations. The Internal Revenue Service (IRS) has established rules that apply to contributions and their limitations.

Review of Service Provider Performance

The Board will conduct periodic reviews of the overall quality of services supplied by the service provider and the service provider's compliance with respect to certain standards of performance. These standards will include, but are not limited to, the timeliness of statements to each plan's participants, accuracy of records being kept and compliance with Plan and Trust documents for both plans.

Oversight of Expenses

The Board will seek to assess the fees necessary to pay for allowable expenses (such as recordkeeping, audit, consultant, and other administrative expenses) in an equal and transparent fashion from participants of the Plans, regardless of the investment options which a participant may select. Any revenue sharing

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credits which are generated from specific investment options will be rebated back to the investment option from which it was generated on a periodic basis. The fees required for both Plan's expenses will then be assessed equally from all participant accounts. Currently, the Board has determined that a pro-rata charge of 0.22% (22 basis points) will be assessed equally across all KPERS 457 participant accounts and an annual fixed rate of \$89 will be assessed to on the account of each KPERS 401(a) participant. The Board will review the fees which are assessed at least annually.

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SECTION 8: Self-Directed Brokerage Services

The self-directed brokerage account is offered to participants of the KPERS 457 plan as a supplemental investment fund to the core investment offerings of the KPERS 457 Plan. It is not available as an investment option for KPERS 401(a) plan assets. The self-directed brokerage account is intended for KPERS 457 plan participants that are interested in a wider array of investment funds and are willing to accept the additional risks associated with those funds.

The Board has no responsibility for selecting, monitoring or evaluating the investment funds available through the self-directed brokerage services. Participants will have sole discretion with regard to the investment funds they select in the brokerage window.

Under the self-directed brokerage account, the plan participant will be responsible for the on-going research, trading and risk management responsibilities associated with their specific investment choices. The maximum allowed cumulative transfer from a participant's account is limited to 50% of a participant's total account value in the Plan. Account balances must have a minimum of \$5,000, with an initial transfer of at least \$2,500 and subsequent transfers in \$2,500 increments.

Available Investment Alternatives

1. Mutual Funds
 - a. Load Mutual Funds
 - b. No-Load Mutual Funds

Unavailable Investment Alternatives

1. Currencies
2. Limited Partnerships
3. Tax-Exempt Securities
4. Futures
5. Options

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6. Precious Metals
7. Commodities
8. Margin Borrowing/Trades
9. Core investment funds of the Plans
10. Service provider's funds listed in enrollment materials
11. Collectibles or Physical Assets
12. Individual Stocks

Empower Excessive Trading Policy

PROCEDURES FOR COMPLYING WITH FUND COMPANY MARKET TIMING AND EXCESSIVE TRADING POLICIES

The prospectuses, policies and/or procedures of certain fund companies require retirement plan providers offering their fund(s) to agree to restrict market timing and/or excessive trading ("prohibited trading") in their funds. The following procedures describe how we, as your recordkeeper, will comply with fund company instructions designed to prevent or minimize prohibited trading.

Various fund companies instruct intermediaries to perform standardized trade monitoring while others perform their own periodic monitoring and request trading reports when they suspect that an individual is engaging in prohibited trading. If an individual's trading activity is determined to constitute prohibited trading, as defined by the applicable fund company, the individual will be notified that a trading restriction will be implemented if prohibited trading does not cease. (Some funds may require that trading restrictions be implemented immediately without warning, in which case notice of the restriction will be provided to the individual and plan, if applicable). If the individual continues to engage in prohibited trading, the individual will be restricted from making transfers into the identified fund(s) for a specified time period, as determined by the applicable fund company. Individuals are always permitted to make transfers out of the identified fund(s) to other available investment options. When the fund company's restriction period has been met, the individual will automatically be allowed to resume transfers into the identified fund(s).

Additionally, if prohibited trading persists, the fund company may reject all trades initiated by the plan, including trades of individuals who have not engaged in prohibited trading.

Note: certain plan sponsors have or may elect to implement plan level restrictions to prevent or minimize individual prohibited trading. To the extent that such procedures are effective, we may not receive requests for information from the fund companies or requests to implement the restrictions described above.