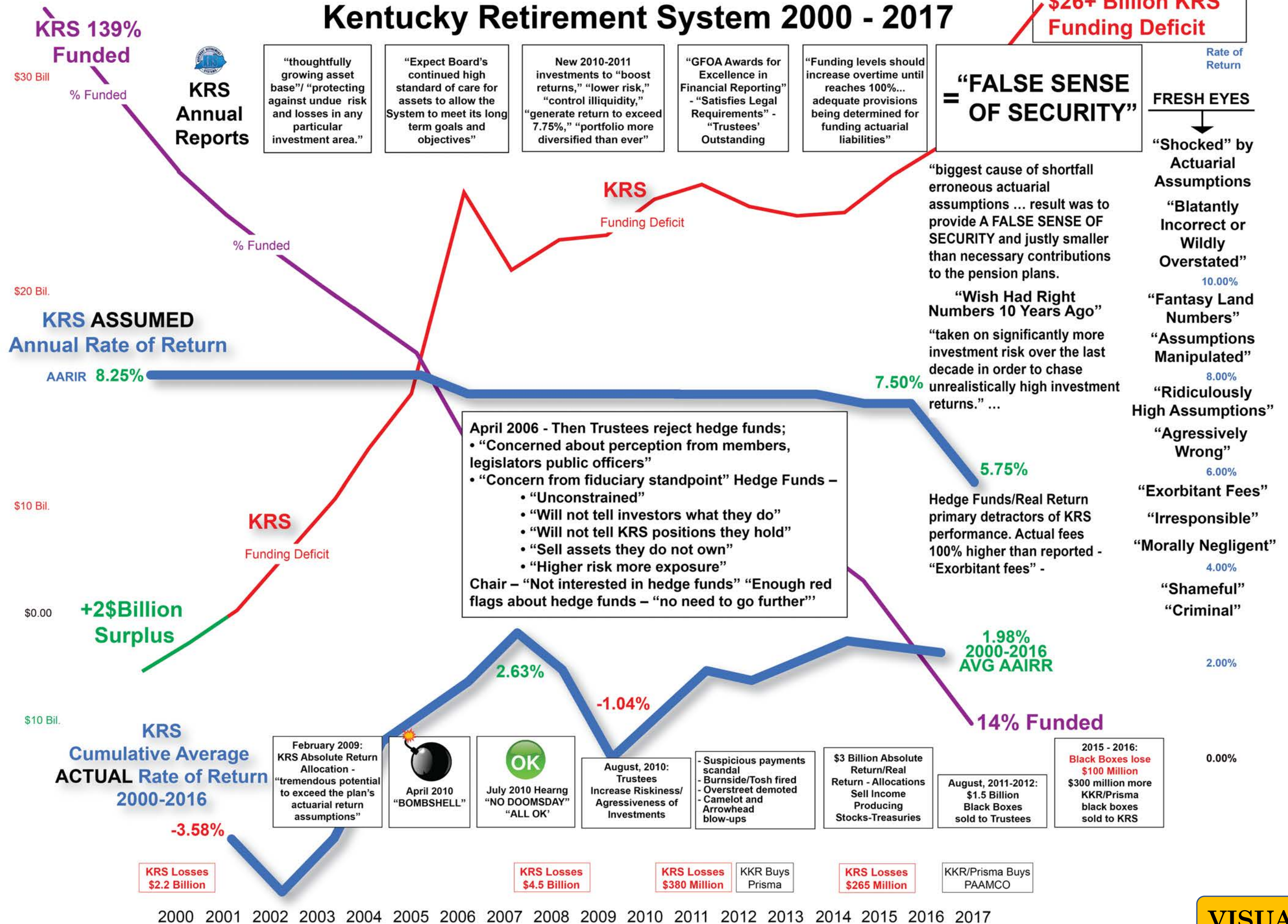
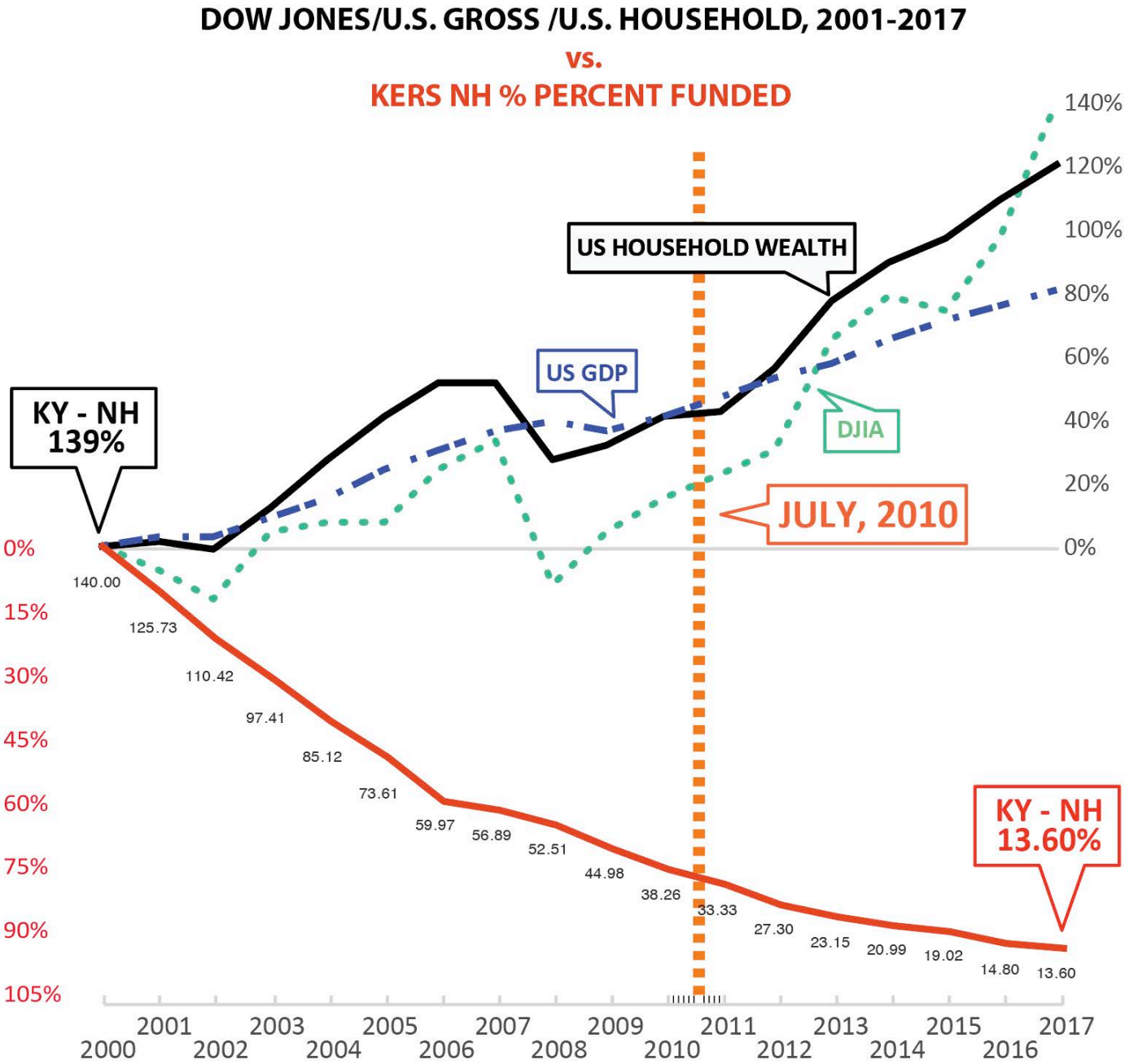


Kentucky Retirement System 2000 - 2017

\$26+ Billion KRS Funding Deficit



KRS-NH vs. OTHER PUBLIC PENSION PLANS



FAC ¶ 28

Pension Fund	% Funded	Pension Fund	% Funded	Pension Fund	% Funded
Connecticut Municipal	86%	Missouri Local EES	95%	Sacramento Co. ERS	87%
Delaware State EES	89%	Missouri PEERS	86%	South Dakota EES	100%
TENN	93%	Missouri Teachers	86%	South Dakota EES	100%
Florida Retirement System	85%	Montana County EES	92%	Texas County	88%
Houston Fire Fighters	86%	Nebraska School EES	90%	Texas Court EES	88%
Iowa PERS	84%	New York State Teachers	87%	Texas Teachers	86%
Los Angeles Fire and Police	94%	North Carolina Local	95%	Washington School EES /Teachers	88-92%
Louisiana State Parochial	99%	North Carolina EES	91%	Washington, DC P&F	110%
Maine Local Govt. EES	86%	Oklahoma PERS	93%	Washington, DC Teachers	91%
Milwaukee City ERS	95%	Oklahoma Police	99%	Wisconsin EES	100%
Minnesota Police and Fire	88%	Pennsylvania Municipal	100%	KERS NH	13.6%

FAC ¶ 213



Kentucky Pension Systems

Investment Underperformance and Growth of Investment Risk

The KRS ... plans have taken on **significantly more investment risk over the last decade** in order to **chase unrealistically high investment returns**. Portfolio allocations to fixed income investments have fallen, while **investments in ... alternatives and hedge funds have increased**.

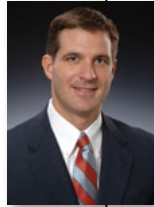
KRS increased [its] alternative investment holdings over the past 15 years and reduced [its] low-risk, fixed-income holdings.

...allocation to riskier alternative investments ... nearly double the peer average.

MANIPULATION OF ACTUARIAL ASSUMPTIONS

Rate of Return: 7.75% - Employee Growth: 4.5% - Inflation 3.25%

Shocked ◦ **Assumptions Ridiculously High** ◦ **Blatantly Incorrect** ◦ **Wildly Overstated** ◦ **Aggressively Wrong** ◦ **Fantasy Numbers**



The massive [increased deficit numbers] are largely a result of new assumptions [which] replace[d] **optimistic [assumptions]** used by boards in the past that caused [KRS] to not ask for sufficient funding, which led to the **accumulation of billions in unfunded liabilities....**

*Lots of complaints about the right numbers.... **I wish they were given the right numbers 10 years ago.*** C-J 12.7.17



KRS made serious math errors in recent years by relying on **overly optimistic assumptions** about its investment returns, the growth of state and local government payrolls, and the inflation rate.... *It doesn't make any sense. We wonder why the plans are underfunded.... **It's the board's responsibility to give the correct numbers....*** H-L 2.16.17



*...past **assumptions** were often **manipulated** by the prior boards in order **minimize the "cost"** of pensions to the state budget. **Unreasonably high investment expectations** were made, and funding was based on false payroll numbers.*

*The result was to provide a **false sense of security** and **justify smaller than necessary contributions** to the pension plans. This was a morally negligent and irresponsible thing to do.* L.Biz.J. 8.29.17



*...**lack of realistic and rational** actuarial assumptions helped **obscure** the distressed financial status of the plans and **contributed** to the long-term unsustainability of the plans.* KY.GOV.com 11.14.17



*We (at KRS) have been aggressive in our assumptions for many years – **aggressively wrong.** And we wonder why we're underfunded....* H-L 5.18.17

Were any of you paying attention? H-L 2.16.17



*What has been done in our pension systems has been **criminal.** It has been **negligent,** it has been **irresponsible** and it is **shameful...** ...if these were private companies they would have been taken over and frozen and disbanded....* H-L 8.25.17

THIS IS MORE THAN NEGLIGENCE
Intentional Wrongdoing of Some Kind
Willful – Reckless – Bad Faith – Deliberate Manipulation


FAC ALLEGATIONS

- Willful/Reckless/Deliberate/Manipulation **alleged 14 times in FAC**
 - Trustees ***actively concealed*** their wrongdoing ¶281,49
 - Trustees **willfully or recklessly violated their duties** to KRS and the taxpayers and **did not act in good faith or in what they honestly believed was in the best interests of KRS by FAILING TO:**
 - **safeguard the trust funds under their control**
 - **invest the trust assets prudently**
 - **avoid excessive and/or unreasonable fees and expenses**
 - **use realistic assumptions actuarial and future investment returns**
 - **protect KRS' full legal rights**
 - **make truthful, disclosure of, the true condition the KRS Funds. ¶174, 281**
- AND BY ASSUMING**
- **4.5% yearly payroll growth when hiring rates were zero/declining**
 - **7.75% of AARIR when cumulative moving average annual rate of return of KRS funds never even came close to that.**
 - **Not a mistake/bad estimate. It is deliberate, willful manipulation to conceal the true financial and actuarial condition and underfunded status of the KRS plans. ¶169.**

CULPABLE TRUSTEES OUSTED
FACTS COME OUT


MANIPULATION OF ACTUARIAL ASSUMPTIONS
Rate of Return: 7.75% - Employee Growth: 4.5% - Inflation 3.25%

Shocked • Assumptions Ridiculously High • Blatantly Incorrect • Wildly Overstated • Aggressively Wrong • Fantasy Numbers




The massive [increased deficit numbers] are largely a result of new assumptions [which] replace[d] **optimistic [assumptions]** used by boards in the past that caused [KRS] to not ask for sufficient funding, which led to the accumulation of billions in unfunded liabilities....

Lots of complaints about the right numbers.... I wish they were given the right numbers 10 years ago. C-1 12.7.17




...past **assumptions** were often **manipulated** by the prior boards in order to minimize the "cost" of pensions to the state budget. **Unreasonably high investment expectations** were made, and funding was based on false payroll numbers.

The result was to provide a **false sense of security** and **justify smaller than necessary contributions** to the pension plans. This was a **morally negligent and irresponsible thing to do.**
L Biz.J. 8.29.17




We (at KRS) have been aggressive in our assumptions for many years – **aggressively wrong.** And we wonder why we're underfunded..... H-L 5.18.17


Were any of you paying attention?
H-L 2.16.17



KRS made serious math errors in recent years by relying on **overly optimistic assumptions** about its investment returns, the growth of state and local government payrolls, and the inflation rate.... *It doesn't make any sense. We wonder why the plans are underfunded.... It's the board's responsibility to give the correct numbers....* H-L 2.16.17



...**lack of realistic and rational actuarial assumptions** helped obscure the distressed financial status of the plans and contributed to the long-term unsustainability of the plans.
NY GOV.com 11.14.17



What has been done in our pension systems has been **criminal.** It has been **negligent,** it has been **irresponsible** and it is **shameful...**
...if these were private companies they would have been taken over and frozen and disbanded.... H-L 8.25.17

This is not a mistake or a bad estimate. It is deliberate, willful manipulation to conceal the true financial and actuarial condition and underfunded status of the KRS Plans. ¶169

CAVANAUGH MACDONALD – ACTUARY ¶139, 145

False assumptions – False Statements – False Sense of Security



NO ONE WAS MORE WRONG ABOUT MORE THINGS THAT MATTER MORE

The firm's actions helped hide the true pension costs and liabilities from Kentucky taxpayers. ~Farris

- Certified actuarial assumptions in Annual Reports *in accordance with the recommendations of the actuary.* Calculated the actuarial liabilities. – *the current actuarial condition of [KRS] ... ¶135,140.*
- Reviewed/Approved false Annual Report ¶300
- *funding level should increase over time to 100% – Adequate provisions being determined for funding actuarial liabilities ¶263*
- If the true actuarial liabilities and lower AARIR were disclosed, – uproar. Cav/Mac terminated, costing them fees. ¶142. Let deception continue. It served their selfish economic purposes to do so. ¶144, 300.
- Knowingly aided and abetted Trustees; participated in a scheme, civil conspiracy, common course of conduct and joint enterprise with Trustees and other defendants. ¶145, 300

WHEN TRUTH DID COME OUT – THEY WERE KICKED OUT
¶144, 300



[T]he trillions of dollars held in pension plans are an enticing target for intermediaries and service providers who are opportunistic, desperate or just plain greedy.

Dana M. Muir, "DECENTRALIZED ENFORCEMENT TO COMBAT FINANCIAL WRONGDOING IN PENSIONS; WHAT TYPE OF WATCHDOGS ARE NECESSARY TO KEEP THE FOXES OUT OF THE HENHOUSES," 53 Am. Bus. L.J. 33, 34 (2016).

RVK – INVESTMENT ADVISOR

False assumptions – False Statements – False Sense of Security

KRS ANNUAL REPORTS



- Prepared April 2010 Bombshell Report. PCM#2
- Advised Trustees to do business with Hedge Fund Sellers with out adequate inquiry and to put \$1.8 billion in Black Boxes even though highly aggressive/risky/exorbitant fees.
- Made false statements regarding KRS' investing practices in KRS Annual Reports, falsely reassuring members and taxpayers as to Trustees' stewardship. ¶136, 301:

*The asset-liability study assisted the Board with deciding on the **most effective asset allocation strategies ... to lower risk, control the level of illiquidity in the portfolios, and generate a return expected to exceed the actuarially assumed rate of return of 7.75% ... the Board has been transitioning to the new ... asset allocations – in a prudent manner.***

- Knew if true investment practices, AARIR and risks of these Black Boxes were disclosed – uproar -- could have been fired – lose fees. Let the deception continue – served their selfish economic purposes to do so. ¶134
- Knowingly aided and abetted the Trustees, while participating in scheme, civil conspiracy, common course of conduct and joint enterprise acting in concert with other defendants. ¶138, 300

WHEN TRUTH DID COME OUT – THEY WERE KICKED OUT
¶137, 301.



Jim Voytko

[T]he trillions of dollars held in pension plans are an enticing target for intermediaries and service providers who are opportunistic, desperate or just plain greedy.

Dana M. Muir,
“DECENTRALIZED
ENFORCEMENT TO COMBAT
FINANCIAL WRONGDOING IN
PENSIONS; WHAT TYPE OF
WATCHDOGS ARE
NECESSARY TO KEEP THE
FOXES OUT OF THE
HENHOUSES,” 53 Am. Bus.
L.J. 33, 34 (2016).

ICE MILLER FIDUCIARY REVIEW CONSULTANTS

False assumptions – False Statements – False Sense of Security



[T]he trillions of dollars held in pension plans are an enticing target for intermediaries and service providers who are opportunistic, desperate or just plain greedy”.

Dana M. Muir,
“DECENTRALIZED
ENFORCEMENT TO COMBAT
FINANCIAL WRONGDOING IN
PENSIONS; WHAT TYPE OF
WATCHDOGS ARE
NECESSARY TO KEEP THE
FOXES OUT OF THE
HENHOUSES,” 53 Am. Bus.
L.J. 33, 34 (2016).

KRS ANNUAL REPORTS

- Fiduciary overseer/monitor/police.
- Ice Miller also had extensive expertise and experience for pension plan trustees including advising on the purchase of fund of hedge fund investments ¶147:

“We represent ... public retirement systems ... [our] **Alternative Investments Group offers a broad range of legal advice and services ... in connection with [public funds] alternative investment programs; we have advised these clients in the collective investment of billions of dollars ... [we] have significant experience evaluating,**

We also regularly advise our institutional investor clients regarding the protection of their alternative investments.

clients regarding the protection of their alternative investments.

- What were the doing when HFS preyed on Trustees?
- Ice Miller **continued** to violate its duties to KRS by permitting in 2015-2016 a KKR/Prisma executive, still paid by KKR/Prisma to work inside KRS, with access to confidential information and the ability to wield influence. ¶151
- Fiduciary police should have stopped – instead \$300 million more purchased – self-dealing in front of Ice Miller. Very type of self dealing by *Fiduciaries* the Fiduciary Consultant/Police to prevent.
- Knew KRS Annual Reports misleading. Knew if the true nature and risks of high-risk, high-fee vehicles and false actuarial assumptions were disclosed would create uproar. Wanted to keep KRS as a client – willing to over look breaches of fiduciary duty to get fees. Let deception continue because it served their selfish economic purposes to do so. ¶302, 148
- Ice Miller knowingly aided and abetted the breach of duties by Trustees, while participating by committing overt acts, in an ongoing scheme, civil conspiracy, common course of conduct and joint enterprise acting in concert with Trustees. ¶153.



GOVERNMENT FINANCE OFFICERS ASSOCIATION ANNUAL REPORT CERTIFIER

False assumptions – False Statements – False Sense of Security

THROUGH REVIEW BY EXPERTS

- “GFOA sponsors award program to encourage sound financial reporting for ... the Comprehensive Annual Financial Report, ...” ¶154

“Reports submitted to the CAFR program are reviewed by selected members of the GFOA professional staff and the GFOA Special Review Committee which comprises individuals with expertise in public sector financial reporting and includes financial statement preparers, independent auditors, academics and other finance professionals.” ¶154

- KRS had to submit a detailed application about the KRS Plans’ finances, investments and practices, as well as the annual report it sought to have certified. ¶155

- Certificate of Achievement in financial reporting review process *typically requires an additional 4 to 6 months.* ¶155

Excellence in financial reporting



Satisfies applicable legal requirements



Annual Reports represented that because of the trustees’ *outstanding stewardship*, KRS had received prestigious award for *Excellence in Preparation of its financial reports*” and publishing Annual Report which “*satisfies applicable legal requirements.*” ¶264

FEATURED IN EVERY ANNUAL REPORT, OFTEN ON THE SAME PAGE AS THE PICTURES OF THE TRUSTEES. ¶265 *OUTSTANDING STEWARDSHIP*

COMMERCIAL ENTERPRISE

- GFOA commercial enterprise/charges public pension fund fees in return for issuing its Certificates – *rubber stamp* ¶266, 303
- Hands out prestigious-sounding/looking certifications – no real research or investigation, nor any skeptical, detailed, independent review or evaluation. business model - - selling a large volume of public pension funds /certificates/endorsement and awards ¶156
- GFOA knew KRS Annual Reports false, and misleading. ¶266, 303
- If GFOA withdrew the certification, this would have raised red flags -- caused uproar -- threatened GFOA’s -- “hand-out-the-certification” -- let the deception continue because it served its selfish economic interests ¶158, 303

[T]he trillions of dollars held in pension plans are an enticing target for intermediaries and service providers who are opportunistic, desperate or just plain greedy.

Dana M. Muir, “DECENTRALIZED ENFORCEMENT TO COMBAT FINANCIAL WRONGDOING IN PENSIONS; WHAT TYPE OF WATCHDOGS ARE NECESSARY TO KEEP THE FOXES OUT OF THE HENHOUSES,” 53 Am. Bus. L.J. 33, 34 (2016).

2016 KKR/PRISMA \$300 MILLION SALE

KENTUCKY RETIREMENT SYSTEMS CONFLICT OF INTEREST AND CONFIDENTIALITY POLICY

Statement of Conflict of Interest and Confidentiality Policy:

Individuals associated with KRS must not engage in activities that have the potential to become a conflict of interest with their association with KRS. ... individuals associated with KRS must not release information about KRS ... that would breach any duty to protect such information.

Purpose:

The purpose of this Conflict of Interest and Confidentiality Policy is to: a) establish what individuals are subject to conflict of interest provisions of KRS; b) establish the specific standards of conduct with regard to conflict of interest; c) establish standards with regard to the confidentiality of information ...

PROCEDURES REGARDING CONFLICTS OF INTEREST AND CONFIDENTIALITY

Section 1: Application of Policy

(1) **This policy shall apply to all individuals who have a statutory, contractual or working relationship with KRS.**

(2) Individuals affected by this policy shall include, but are not limited to:

- a. **Employees of KRS;**
- b. KRS Trustees;
- c. **Independent contractors of KRS;** and
- d. **Vendors of KRS.**

Section 2: Standards of Conduct Regarding Conflicts of Interest

1. Individuals have an obligation to **diligently** identify, disclose, avoid, and manage conflicts of interest.
2. Potential conflicts of interest exist when an individual ... **may be directly or indirectly financially impacted**, ... by a decision made by KRS in which the individual participates....
5. **Individuals should not conduct business or participate in decisions with a company or agency in which the individual ... is employed....**
7. **Individuals must avoid all conduct which in any way might lead the public to believe that the individual is using his or her position with KRS to further private interest.**

Section 3: Standards of Conduct Regarding Confidentiality

1. **Individuals associated with KRS may be granted access to confidential information** in the course of employment, KRS Trustee, or within a contractual relationship with KRS....
3. **These individuals have a duty to keep confidential the information** to which they are granted access as a result of their association with KRS.

INDIVIDUALS ASSOCIATED WITH KRS PROHIBITED FROM:

- using *KRS confidential information* to further his/employer's economic interests
- participating in decisions involving company employing individual
- having direct/indirect interest in gains/profits of any investments by KRS board

61.655 BOARD OF TRUSTEES – CONFLICT OF INTEREST

No trustee or **employee** of the Kentucky Retirement Systems board shall:

- (1) Have any interest, direct or indirect, in the gains or profits of any investment or transaction made by the board, ...
- (2) Directly or indirectly, for himself or as an agent, use the assets of the retirement system, except to make current and necessary payments authorized by the board...
- (6) Use confidential information acquired during his or her tenure with the retirement system to further his or her own economic interests or that of another person; or
- (7) **Hold outside employment with, or accept compensation from, any person or business with which he or she has involvement as part of his or her official position with the retirement system ...**

KKR/PRISMA/PAAMCO 2016 \$300 MILLION BLACK BOX SELF-DEALING TRANSACTION



KRAVIS



ROBERTS



REDDY



BUCHAN



PEDEN



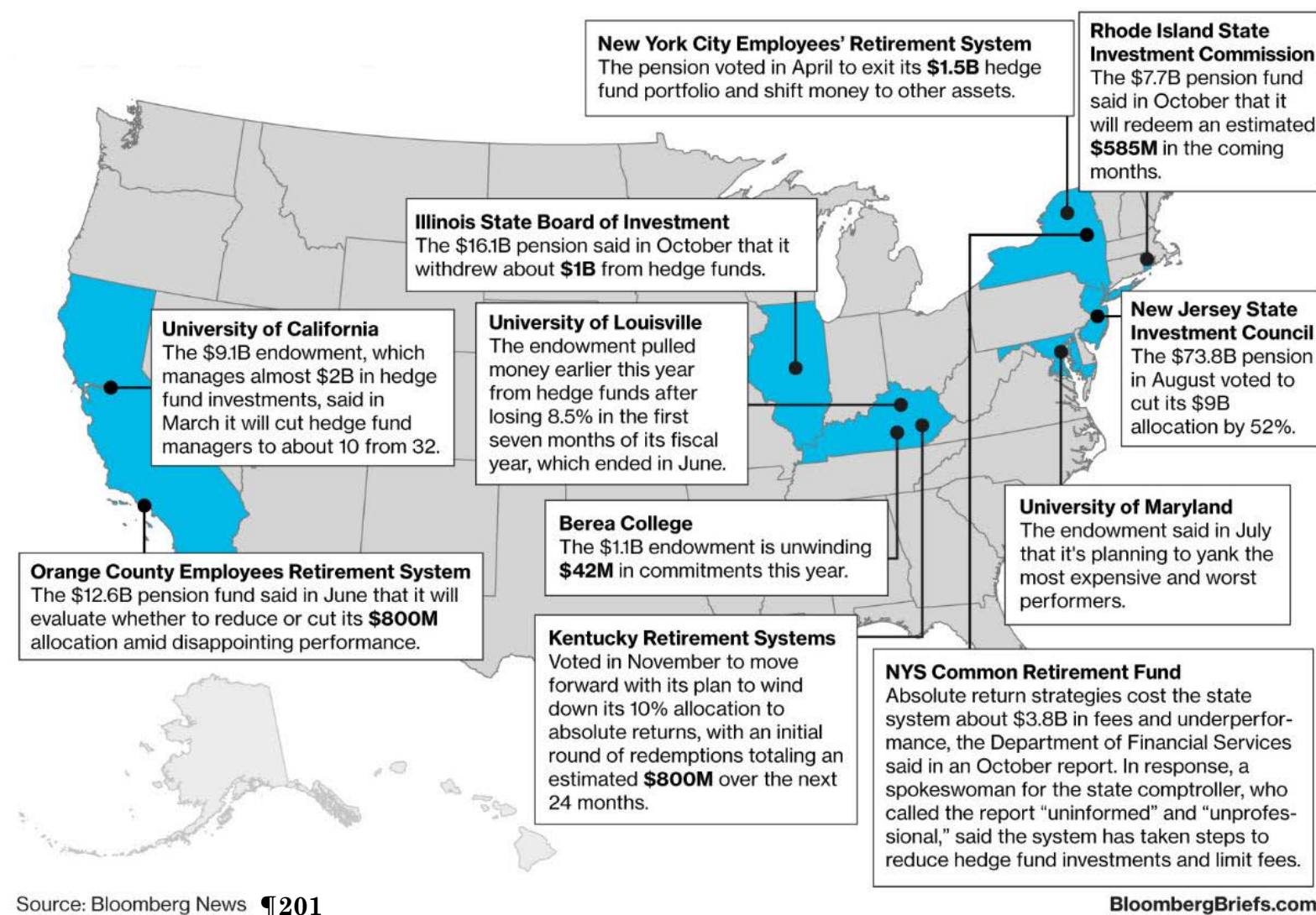
KKR MYSTERY MAN

WHAT WAS DONE

- Black Boxes lose \$100 million 2015-16
KKR/Prisma biggest loser
- Peden - Formerly Prisma/now KRS CIO
- KKR/Prisma –
 - **Mystery KKR/Prisma employee inside KRS**
 - Stays on KKR/Prisma payroll
 - Peden: *free staff member, extension of our staff*
 - part of **partnership** with KKR/Prisma
- 2015-16 pension fund redemptions resulting from excessive hidden fees, poor returns/large losses – fund of hedge funds industry severely contracted – \$100 billion **hedge fund industry – an industry in crisis**
- **\$300 million more Daniel Boone Fund** – worst performer/biggest loser – KRS owns \$800 million – **5% of total fund assets** – **extreme self-dealing**

¶ 88-92, 199-202

2015-16 MASSIVE HEDGE FUND REDEMPTIONS SWAMP INDUSTRY



WHY WAS THIS DONE?

- KKR/Prisma, Roberts, Kravis, Reddy and Peden arrange for KKR/Prisma Executive to work inside KRS while still being paid by KKR/Prisma to protect KKR/Prisma's hold on KRS. ¶ 87-91, 199-202
- KKR/Prisma needed new hedge fund business in 2015-16. Acquiring PAAMCO – more “AUM” helps acquire PAAMCO ¶ 75 Negotiated and approved by Kravis, Roberts, Reddy - **personal involvement** ¶ 87-91
- While Peden and KKR/Prisma executive working together inside KRS, and using this position plus confidential information, KKR/Prisma sold \$300 million more to KRS (**despite fact that KKR/Prisma's Black Box was the worst performing of the three**), which helps KKR/Prisma in PAAMCO negotiations. ¶ 201
- **VIOLATED KPL – KRS CONFLICTS POLICY** –
- This very large sale was a significant benefit to KKR/Prisma
- Investment **not done solely in the interest of or for the exclusive purpose of providing benefits to members, but to help KKR/Prisma acquire PAAMCO on better terms.** ¶ 201
- **SELF-DEALING WITH TRUST ASSETS – MIS-USE OF KRS CONFIDENTIAL INFO**
- **VIOLATES 61.645 KRS CONFLICT POLICY**
- **PUNITIVE DAMAGES**

THE BIG THREE

IMPLIED FIDUCIARY DUTIES – AIDING/ABETTING – JOINT/SEVERAL LIABILITY

CORPORATE OFFICER LIABILITY – CULPABLE ACTORS’ DOMINATION TOLLS S/L

STEELVEST v. SCANSTEEL (1991)*

Person who **knowingly joins or aids and abets a fiduciary** in an enterprise constituting a **breach** of the fiduciary relationship becomes jointly and severally liable with the fiduciary. Third person who participates in the violation of duty may be liable to the beneficiary.

One who knowingly aids, abets, or joins fiduciary in the breach of his duty in order to make a profit becomes jointly liable.

Circumstances which may create a fiduciary relationship are so varied it is impossible to create a comprehensive definition.

General rule: such relationship is founded on trust or confidence reposed by one in the integrity and fidelity of another.

It exists in all cases where there has been a special confidence reposed in one who in equity and good conscience is bound to act in good faith and with due regard to the interests of the one reposing confidence.

SMITH v. ISSACS (1989)*

Agent of a corporation is **personally liable** for a tort committed by him although he was acting for the corporation.

Liability attaches to third persons, regardless of the corporate entity, for personal negligence in management and supervision of corporate employees and corporate activities ...

Personal liability attaches for **conducting an activity through servants or agents if one is negligent or reckless in supervision.**

WILSON v. PAINE (2009)*

Where injury not immediately discoverable, courts steer away from the unfairness inherent in charging a plaintiff with slumbering on rights not reasonably possible to ascertain.

Adverse domination shares the same theoretical underpinnings as the discovery rule as applied in the corporate context and provides: ***cause of action will be tolled during the period that a plaintiff corporation is controlled by wrongdoers.***

This doctrine is rooted in principles of agency law premised on the notion that knowledge of agent is not imputed to principal if agent is acting adversely to interests of principal: *corporation is the principle and board as a whole is agent. When board is accused of breaching duty to corporation, it necessarily is accused of acting adversely...*

To rebut, ***defendants must show that there was someone who had knowledge, ability, and motivation to bring suit during the period of corporate control.***

Adverse domination recognizes the reality of situations involving wrongdoing by controlling directors and officers and corporation’s inability to institute suit to protect it. ***It is applied to toll statutes of limitations in situations when those in power control the information necessary to institute suite on behalf of an injured corporation. These parties cannot be expected to sue themselves or to initiate an action contrary to their own interest.***

*908 S.W.2d 104 (1995). See also *Abbott v. Chesley* 413 S.W.3d 589 (2013) (re“Joint Enterprise”/“Joint Adventure”).

* 777 S.W.2d 912 (1989).

* 288 S.W.3d 284 (2009).

KKR – BLACKSTONE

EXECUTIVE POSITIONS AND PARTNERSHIP STRUCTURES = 100% CONTROL

THEY ARE HANDS-ON EXECUTIVES



Kravis/Roberts Co-Chairmen/CEOs –“actively involved and [have] an intimate knowledge of KKR’s business – KKR depends on the efforts, skills” ¶ 77-78,81

Schwarzman Chairman/CEO: “involved in all phases of the firm’s development since its founding” – “depends on [his] efforts, skills, ... “Hill, C.E.O. of Hedge Fund Solutions group and other senior members of our Hedge Fund Solutions team meet regularly with Mr. Schwarzman to review the group’s business” ¶ 97, 98



LIMITED PARTNERSHIP “CORPORATE” CONTROL PROVISIONS



Only two members of Executive Committee. Managing General Partner of KKR is KKR Management LLC, owned and controlled by Kravis and Roberts. ¶127

- The **management** of KKR’s business is **by the general partner rather than a board of directors**. Managing Partner [Kravis/Roberts] serves as KKR’s sole general partner. Managing Partner **appoints KKR’s other officers**.
- [Managing Partner] **may act without any fiduciary obligations** to holders of KKR common units,... permitted to **make decisions it is sole discretion** ... entitled to **consider only its own interests** – no duty (fiduciary or otherwise to any holder of KKR common units....
- 100% control! ¶79, 120-132

1) KKR and Blackstone -- private partnerships, 2008/2010 went *public*. -- Through private agreements, Kravis and Roberts and Schwarzman, retained 100% legal, managerial and operational control -- so they could continue using entities as personal instrumentalities

¶123, 124

2) Limited Partnerships look like *public* companies but they are personal vehicles of Kravis, Roberts and Schwarzman. Legal, operational and managerial control of Kravis, Roberts, and Schwarzman is such that these entities are their personal instrumentalities and *alter egos*. ¶130

3) The corporate jurisdictional contacts of KKR/Blackstone with Kentucky are attributable to both Kravis and Roberts and Schwarzman personally as they are the *jurisdictional alter egos* of KKR/Blackstone ¶180

4) Kravis/Roberts, Schwarzman as responsible corporate officers, had a duty to **train** officers and employees in duties of good faith, care, compliance with applicable public pension laws, and fiduciary duties and *supervise* them.

- Schwarzman ***Chairman of our general partner.... Blackstone Management ... controlled by our founder, Mr. Schwarzman.***
- Blackstone Management [Schwarzman] manages **all of our operations and activities ... is authorized to perform all acts to conduct our business ... general partner in managing operations is**
- Entitled to **consider only ... its own interests ... no duty (fiduciary or otherwise) to ... any limited partners,...**
- Schwarzman is Blackstone’s general partner and “**manages all of its operations and activities**” ***as he desires in his own interests.***
- 100% control. ¶98, 120-132



UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K

The Blackstone Group L.P.

“Blackstone,” the “Partnership,” “we,” “us” or “our” **refer to The Blackstone Group L.P.** and its consolidated subsidiaries. ...
“Blackstone Funds,” “our funds” and “our investment funds” refer to the ... funds of hedge funds ... and registered investment companies that are managed by Blackstone.

Blackstone is a leading global alternative asset manager ... **Our alternative asset management businesses include** investment vehicles focused on ... **hedge fund solutions**....

Our investment funds ... advised by a **Blackstone entity** serving as investment adviser that is registered under the U.S. Investment Advisers Act of 1940, or “Advisors Act.” ...

All of the investment advisors of **our** investment funds operating in the U.S. are registered as investment advisers with the SEC ...registered investment advisers are subject to the requirements and regulations of the Advisers Act [including] fiduciary duties to clients.

Lee Dec ¶12 reference to
“KKR/Prisma” in 10-K “is not to a
combined company”
BUT SEE



UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K
KKR & CO. L.P.

Lee Dec ¶4 “KKR has not registered with
the [SEC] as an investment adviser. KKR
has not provided investment advice to
KRS.” **BUT SEE**

In this report, references to “KKR,” “we,” “us,” “our” and “our partnership” **refer to KKR & Co. L.P.** and its consolidated subsidiaries.

We are a leading global investment firm that manages investments across multiple asset classes including ... hedge funds.

Our hedge fund business is comprised of customized hedge fund portfolios, hedge fund-of-fund solutions and direct hedge funds managed by **KKR Prisma** ... Within **our** hedge funds business, ... KKR Prisma managed \$9.9 billion of AUM ...

We conduct **our** advisory business through **our** investment adviser subsidiaries, [including] **Kohlberg Kravis & Roberts**, and its wholly owned subsidiaries ... Prisma Capital Partners LP, **each of which is registered as an investment adviser with the SEC under the Investment Advisers Act.** The investment advisers are **subject to ... fiduciary duties**....

HEDGE FUND SELLERS’ LLC AGREEMENTS – INCONSISTENT AND HELPFUL TO PLAINTIFFS

KKR
PRISMA
KKR/PRISMA LLC
LIMITED LIABILITY COMPANY
AGREEMENT
DANIEL BOONE FUND LLC

Section 2.3 Limitation of Liability; Indemnification.
The Manager or Manager Affiliate shall not be liable for damages, for losses sustained...by...KRS, if the Manager **did not act fraudulently or in bad faith or with willful misconduct or with gross negligence or otherwise breach the standard of care set forth in Section 2.4.**

Section 2.4 Standard of Care.
...the Manager will comply with **all** applicable laws and regulations, ... will exercise the care, skill, prudence and diligence under the circumstances ... [of a] reasonably prudent person ... **The Manager agrees that it owes fiduciary duties and responsibilities to KRS...**

Section 2.2 Powers of the Managers.
(m) Manager will comply with...the Statement of Investment Objectives, Policies, and Guidelines of Kentucky Retirement Systems...

(u) the Manager will maintain insurance coverage ...

*** “Manager Affiliate(s)” means the Manager, each Person who controls the Manager...and each director, officer...of...or any such controlling...person.**

Blackstone
BLACKSTONE LLC
LIMITED LIABILITY COMPANY AGREEMENT
HENRY CLAY FUND, LLC

Section 2.3 Limitation of Liability; Indemnification.
The Manager and the Manager Associates* shall not be liable to KRS...for any loss, ... any act or omission that is Judicially Determined to be **primarily attributable to fraud, bad faith, willful misconduct or gross negligence of the Manager...**

Section 2.4 Standard of Care. The Manager will comply with all applicable laws and regulations, ... The Manager agrees that it owes fiduciary duties and responsibilities to the Company under the Advisers Act

Section 2.6 Representations, Warranties and Agreement of The Manager.

(m) The Manager, ... agrees to comply with the Statement of Investment Objectives, Policies and Guidelines of Kentucky Retirement Systems.

(s) the Manager acknowledges that KRS reserves all ... rights or actions ... under...applicable Kentucky law...

(u) the Manager currently maintains insurance coverage ...

Section 2.12 Investment policies. The **Manager shall act at all times in accordance with ... the laws of the Commonwealth of Kentucky.**

*** “Manager Associate(s)” means the Manager, each Person who controls the manager ... and each director...officer of...any such controlling person...**

PAAMCO
PAAMCO LLC
LIMITED LIABILITY COMPANY AGREEMENT
NEWPORT COLONELS, LLC

Section 2.4 Limitation of Liability; Indemnification.
... to the extent that, at law or in equity, **the Manager or any Manager Associate*** has duties (including fiduciary duties) and liabilities relating thereto ... shall not be liable, **if the Manager or such Manager Associate did not act fraudulently or in bad faith or with willful misconduct or with gross negligence...**

(j) ... state securities laws impose liabilities ... on Persons who act in good faith, ... nothing in this Agreement waives or limits any rights that ... a Member may have under those laws.

Section 2.3 Powers of the Manager.
(p) the Manager will ... maintain insurance coverage

Section 2.11 Investment Policies. ...Attached ... is the Statement of Investment Policy of the Kentucky Retirement Systems.

EVEN IF LLCs NOT VOIDED
THEY DON’T JUSTIFY
DISMISSAL

Limitation of liability is Not Immunity:

- **fraud/bad faith/will – full misconduct/gross negligence – Pleaded: Predatory Targeting ¶14,17-19,43**
- **Knowingly selling unsuitable investment Excessive Fees ¶164,183**
- **Willful, Wanton, Gross Negligence, Malice ¶319**

LLC’s INCONSISTANT
• **ADMIT FIDUCIARY DUTY/WILL COMPLY KENTUCKY LAW**
• **AGREE TO KRS INVESTMENT POLICY – REQUIRES ASSET MANAGERS TO – ASSUME FIDUCIARY RESPONSIBILITY**



KRAVIS



ROBERTS



SCHWARZMAN



HILL



BUCHAN



REDDY

Kravis, Roberts, Schwarzman, Hill, Buchan, Reddy personally protected under LLC Agreements – personal benefit.

LEGAL DUTIES OF ADVISERS

KENTUCKY PENSION LAW – 61.650 (1)(c):

DUTIES OF FIDUCIARIES

- A trustee, officer, employee, **or other fiduciary** shall discharge duties with respect to the retirement system:
- **Solely in the interest of** the members and beneficiaries;
- For the **exclusive purpose** of providing benefits to members and beneficiaries and and paying **reasonable expenses** of administering the system;

STEELVEST IMPLIED FIDUCIARY DUTY

- Hedge Fund Sellers and Investment, Actuarial and Fiduciary Advisors [Not GFOA] were all **fiduciaries** to KRS and Kentucky taxpayers with **constant access** to non-public information of KRS and its Pension Funds;
- held themselves out to be **highly qualified experts** with extensive experience and expertise to help
- knew the KRS trustees were dealing with **internal turmoil/staff turnover/inexperienced investment staff unusually dependent upon their experience, expertise**
- For Hedge Fund Sellers: because they had **discretion to select the downstream Black Box funds and were also acting investment advisers and/or investment managers for KRS**
- **ELEMENTS** OF IMPLIED FIDUCIARY DUTY – **PLEADED – RAISE FACTUAL ISSUES - ¶164, 287.**

HEDGE FUND SELLERS – FIDUCIARIES AS MATTER OF LAW

- Kentucky law – Investment KRS investment policy – Force of Law – Required then to be fiduciaries
- Representations of Hedge Funds Sellers – 10-Ks PCM#33, 34 - Buchan Presentation PCM#32
- 1940 Investment Advisors Act – Federal law – applies nation wide

ALL DEFENDANTS – CONCERTED CONDUCT CLAIMS

- Defendants **knowingly aided and abetted** the breach of duties by Trustees – **participating in a scheme, civil conspiracy, common course of conduct and joint enterprise.** ¶138, 93.
- Each Defendant played an indispensable part, each taking specific overt acts within their areas of expertise to further the civil conspiracy. ¶293.
- Cover up – continuing wrong doing – continuing mutually supportive acts of each Defendant. **Had any one of them complied with their duties to KRS or the Commonwealth, the damages could have been mitigated or avoided.** ¶293.

“[T]he trillions of dollars held in pension plans are an enticing target for intermediaries and service providers who are opportunistic, desperate or just plain greedy”

Dana M. Muir, “DECENTRALIZED ENFORCEMENT TO COMBAT FINANCIAL WRONGDOING IN PENSIONS; WHAT TYPE OF WATCHDOGS ARE NECESSARY TO KEEP THE FOXES OUT OF THE HENHOUSES,” 53 Am. Bus. L.J. 33, 34 (2016).

KENTUCKY PENSION LAW

Key Statutory Provisions

§61.645(15) BOARD OF TRUSTEES – POWERS

(a) A **trustee** shall discharge his duties as a trustee...

1. In good faith
2. On an informed basis
3. In a manner he honestly believes to be in his best interests.
- In good faith**
- On an informed basis**

(b) A trustee discharges his duties on an informed basis if, **when he makes an inquiry ... into a particular matter, he makes an inquiry ... into a particular matter.**

(c) **action to be taken or decision to be made ...**

1. ...members or employees [or firms] whom the trustee honestly believes to be reliable and competent in the matters presented;
2. ...actuaries, or other persons as to matters the trustee honestly believes are within the person's professional or expert competence; or
3. A committee of the board ... if the trustee honestly believes the committee merits confidence.

(d) A trustee shall **not** be considered as **acting in good faith** if he has **knowledge** concerning the matter in question that **makes reliance** otherwise permitted by paragraph (c) of this subsection **unwarranted**.

(e) Any action taken as a trustee,... shall not be the basis for monetary damages or injunctive relief unless:

1. The trustee has breached or failed to perform the duties of the trustee's office in compliance with this section; and
2. In the case of an action for monetary damages, the breach or failure to perform constitutes willful misconduct or wanton or reckless disregard for human rights, safety, or property.

(f) **A person bringing an action for monetary damages**

pre and the burden of proving that the breach is a failure to pay for use of the legal cause of damages suffered by the Kentucky Retirement Systems

(h) ... a trustee shall strive to administer the retirement system in a **cost-effective manner** **manner for the taxpayers of the Commonwealth of Kentucky.**

§61.650(1) BOARD TRUSTEE OF FUNDS

(c) A **trustee, officer, employee, or other fiduciary** shall discharge duties with respect to the retirement system:

1. Solely in the interests of the members and beneficiaries;
2. For the exclusive purpose of providing benefits to members and beneficiaries and **paying reasonable expenses of administering the system;**
3. With the care, skill, and caution under the circumstances then prevailing that **a prudent person** ... would use....

Solely in the interest of the members and beneficiaries

For the exclusive purpose of providing benefits to members – and reasonable expenses

BUCHAN/PAAMCO – TRUSTED ADVISOR BY JULY 2010

October 2009 - July 2010

From: Jane Buchan [mailto:jane.buchan@paamco.com]
Sent: 10/3/2009 2:08:34 PM
To: Tosh, Adam (KRS) [adam.tosh@kyret.ky.gov]
Subject: RE: Congrats on Arrowhawk....hope all is well....Jane

I am traveling most of October. Actually I am in London on Monday and Tuesday!!! If you want to have a drink, let me know. I am in most of November & December but have to be in London the week of Nov 16 but I believe everything else works.

Congrats again on Arrowhawk -- I am sure it was no small feat!

Best,
Jane

Congrats again on Arrowhawk

Jane Buchan, Chief Executive Officer
Pacific Alternative Asset Management Company
19540 Jamboree Road, Suite 400, Irvine, CA 92612 USA
tel/ +1 949 261 4900 fax +1 949 261 4905
www.paamco.com | jbuchan@paamco.com

Oct. 2009

From: Tosh, Adam (KRS) [adam.tosh@kyret.ky.gov]
Sent: Friday, October 02, 2009 6:51 PM
To: Jane Buchan
Subject: Re: Congrats on Arrowhawk....hope all is well....Jane

Jane:

Appreciate it.

I am heading to London now for a week. But I would like to speak with you upon my return. I still

have considerable work to do with KY's portfolio

I was wonder about availability for a possible trip to LA

Thanks,
Adam
502.545.3734 (mobile)

ARROWHAWK – FIRST
ABSOLUTE RETURN
HEDGE FUND –
WENT BUST – PAYOFFS
INVOLVED

INCREASING RISK
AND
AGGRESSIVENESS OF
INVESTMENTS TO
CHASE HIGHER
RETURNS TO ACCEPT
BLACK BOXES

Phone Call KRS: Brent
Aldridge, interim
CIO
PAAMCO: Jane
Buchan, Managing
Director/CEO

Advice

[Aldridge] has little alternatives experience.
We need to help him *get up the curve fast*
and perform our *trusted advisor service* to
him.... He said ... we are one of only two or
three firms that should get this mandate.

July 15-20, 2010

Filed 17-CI-01348 Amy Feld
Phone Call Brent
Aldridge
Jane
Buchan

7/20/2010 Brent called (first morning as interim CIO). They are
geared up the FORT search ... we come "highly recommended" from
Adam. ... He asked for our advice on ... into their search. ... I ...
suggested that he ask for 4 to 5 references from
each FOHE and personally call each one of

I think he is looking for lots of overall help.
This is his first CIO job.

AUGUST 2010
BUCHAN LOSES LAW-
SUIT –
DECEIT/FRAUD
REVEALED – LOSES
40% OF COMPANY TO
SUSSMAN + \$20
MILLION

TOSH - CIO - FIRED
LEAVES 7/16/16
INTERNAL
IMPROPER
PAYMENTS.

LEGISLATIVE
HEARING 7/21/10

SPECIAL INV.
COMM/BOARD
MEETING 8/12/10

INCREASE
ABSOLUTE
RETURN/BLACK
BOX ALLOCATION:
INCREASE FEES
FOR PAAMCO

BLACKSTONE/PRISMA PRE-SALE INVOLVEMENT WITH KRS

April 2009 - June 2011

Blackstone currently managing
\$160 million of KRS investments
PCM#23; ¶40



Blackstone presentation to KRS board
Nov. 2008 guiding them toward
Blackstone hedge funds PCM#9

SELLER	LOCATION	DATE	KRS STAFF
Blackstone	FUND ON-SITE	March 1, 2010	David
Blackstone	KRS ON-SITE	June 9, 2010	Investment Team
Blackstone	KRS ON-SITE	April 6, 2011	Investment Team
Blackstone	Phone call	May 12, 2011	Investment Team
Blackstone	NYC ON-SITE	June 15, 2011	Tom, TJ, David and RVK
Blackstone	Phone call	June 22, 2011	Tom, TJ, David

PRISMA

Prisma	KRS on-site	April 9, 2009	Investment Team
Prisma	Phone call	April 14, 2009	David
Prisma	FUND ON-SITE	June 17, 2010	Investment Team
Prisma	PHONE CALL	August 25, 2010	Investment Team
Prisma	Phone call	May 19, 2011	Investment Team
Prisma	Fund on-site	June 16, 2011	Tom, TJ, David and RVK

HEDGE FUND SELLERS WERE THERE EARLY – AND LATE FIDUCIARIES BEFORE AND AFTER SALE OF BLACK BOXES

KRS INVESTMENT POLICY

The Board of Trustees authorizes and directs the appointment of an Investment Committee with full power to act for the Board in the acquisition, sale and management of the securities and funds of the Systems in accordance with the provisions of the Statutes and Investment Policy of the Board.

The Investment Committee has the following oversight responsibilities:

* * *

Investment Managers shall be qualified and agree to serve as a fiduciary

Investment Managers shall be qualified and agree to serve as fiduciary to [KRS] ... and discharge their duties ... ***solely in the interest of*** the participants and beneficiaries.

August 2, 2011

PACIFIC ALTERNATIVE ASSET MANAGEMENT COMPANY

Kentucky Retirement Systems
August 2, 2011

“A FIDUCIARY AND SOLUTIONS PROVIDER
committed to understanding and servicing the
needs of our institutional investors” **“M&I”**

Investment Process

SENIOR INVESTMENT PROFESSIONALS



JANE BUCHAN, MA, PhD, CAIA
CEO/Managing Director
Fixed Income Relative Value

Years of Investment Experience: 26
Years at PAAMCO: 11
PhD Harvard University

**“WE BELIEVE
transparency is
inextricably linked to
our fiduciary duty”**

INVESTMENT PHILOSOPHY

“Have a well-established culture of striving to implement best practices as **a fiduciary**”

**“Maintaining
high ethical
standards
AS A
FIDUCIARY”**

**“WE EMBRACE
OUR **FIDUCIARY
DUTY** TO OUR
CLIENTS AND
RECOGNIZE WE
ARE RESPONSIBLE
FOR PEOPLE’S
RETIREMENT ASSETS”**

PAAMCO

MEMORANDUM

RVKuhns & ASSOCIATES, INC.

To: Kentucky Retirement System
From: R.V. Kuhns & Associates, Inc.
Subject: Absolute Return Strategies Fund
Date: August 2, 2011

The KRS Staff engaged RVK to conduct the intent of including them in the appropriate pension and insurance plans.

The Investment Committee recommended approximately \$1.2 billion of the total KRS initially hired FoHF managers to limited partnership structures that put individual strategy monitoring responsibilities on teams dedicated to the hedge fund

The list below details the primary potential absolute return strategy

- Registered Investment Advisor - We require each firm to be a Registered Investment Advisor with the SEC and willing to accept fiduciary responsibility.

We require each firm to be a Registered Investment Advisor with the SEC and willing to accept fiduciary responsibility

As stewards of public funds

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K
The Blackstone Group L.P.

All of the investment advisers of **our** investment funds operating in the U.S. are **registered investment advisers with the SEC ... subject to requirements and regulations of the Advisers Act** [including] **fiduciary duties to clients.**

We conduct **our** advisory business through our investment adviser subsidiaries ... **each of which is registered as an investment advisor with the SEC ... subject to ... fiduciary duties**

Our hedge fund business is comprised of customized hedge fund portfolios, hedge fund-of-fund solutions and direct hedge funds managed by **KKR Prisma** ... Within **our** hedge funds business, as of December 31, 2016, KKR Prisma managed \$9.9 billion of AUM ...

We conduct **our** advisory business through **our** investment adviser subsidiaries, [including] **Kohlberg Kravis & Roberts**, and its wholly owned subsidiaries ... Prisma Capital Partners L.P., each of which is registered as an **adviser** with the SEC under the Investment Advisers Act. The investment advisers are **subject to ...**

BEFORE TOSH-RVK-BUCHAN/PAAMCO-KKR/PRISMA-BLACKSTONE ARRIVE ON SCENE
KRS REJECTS HEDGE FUNDS

April 24, 2006
KRS INVESTMENT COMMITTEE

Discussion to determine whether to explore Hedge Funds further:

- *Need to be concerned about the **PERCEPTION** from members, legislators, or other public officials.*
- *Concern from **FIDUCIARY STANDPOINT** - hedge funds **UNCONSTRAINED**.*
- *Problem is that **FUNDS WILL NOT TELL INVESTORS** what they do [or] **KRS WHAT POSITIONS THEY HOLD**.*
- Hedge funds **SELL ASSETS THEY DO NOT OWN**.
- **HAVE HIGHER RISK AND EXPOSURE.**

CONCLUSION

- ***ENOUGH RED FLAGS ABOUT HEDGE FUNDS – NO NEED TO GO ANY FURTHER.***
- ***NOT BE INTERESTED IN HEDGE FUNDS***

PCM#8



**Executive Summary
Asset/Liability Study
Kentucky Employees Retirement System
Non Hazardous Pension Fund***



April 2010

KRS ... faces an appreciable risk of running out of assets

... complete exhaustion of the fund's assets in seven to ten years....

...no reasonable investment strategy ... that would allow plan to *invest its way to significantly improved financial status* ... without ... courting substantial risk....

...that risk, once taken, may lead ... to the fastest depletion of the plan's assets....

...adoption of a significantly more aggressive investment strategy.... the aggressive approach ... substantially increases the chances of the catastrophic event of depleting all assets in the near future....

This decision is not an investment decision per se. **It is a funding decision....**



***Results similar for all funds. BT June, 2011; July 21, 2010 Legislative Hearing.**

July 21, 2010 LEGISLATIVE SUB-COMMITTEE HEARING



James Voytko,
RVK



Brent Aldridge
KRS Acting CIO



Michael Cherry, Co-Chair
of Joint Committee on
State Government,
Sponsor HB-1



Michael Burnside,
Former Executive
Director of KRS.



**NO DOOMSDAY PREDICTED
NOT GOING BROKE
WILL REMAIN VIABLE**

Voytko (Hearing Transcript p. 22.)

...I don't mean to be a doomsday predictor. That's not the most likely case ... most likely case is that [when] ... HB-1 contributions start to rise ... you actually have positive cash flows.

Cherry/Voytko (Hearing Transcript, pp. 27-29)

...HB-1 is not ceiling... It's a floor. ... as long as we [make HB-1 payments], we're not going to go broke and we're going to meet our obligations ... we're going to be okay ... **if you, in fact, do make those graduated payments, you're not going to run out of money and the system is going to remain viable** ... as long as we do that ... we're not going to go broke. Fair statement?
VOYTKO: ... **yes.**

**NO LEGISLATIVE ACTION
REQUESTED OR REQUIRED**

Cherry (Hearing Transcript p. 30.)

...is there anything else we can do?

Voytko (Hearing Transcript p. 30.)

...that involves a legal opinion, which we would never venture to give you.

Cherry/Burnside (Hearing Transcript p. 34.)

...you're not trying to tell us that next year we should do another HB-1 ... for example?
MR. BURNSIDE: **No, sir.**

“False Sense of Security”

**KRS FACED NO DANGER
OF DEPLETING ITS ASSETS**

Voytko (Hearing Transcript p 14.)

...we in the nation ... all investors ... face an investment environment ... that's quite adverse ... **an extreme situation** ... **a number of adverse years** ... over the next 20 years, it is possible that the fund's assets could, in fact, be depleted ... **we are not predicting it** ...

7.75% AIIRR IMPOSSIBLE

Voytko (Hearing Transcript pp 14, 19, 22.)

...the expected 7.75 percent simply never happens in the real world of investing ... it is very, very difficult, if not impossible, for pension plans to earn 7.75 percent
...While we are assuming ... 7.75% ... we know that's not the real world.

Scheme/Cover up Common Enterprise Starts – KRS Portfolio Reshaped to Accept Hedge Fund Sellers' High Risk/High Fee Products

2010

April

May

June

July

August

**MAY
KRS INV COMM & BOARD MEETINGS**

April 2010 bombshell report presented

**JUNE 22
INVESTMENT COMMITTEE MEETING**

- “preserving liquidity of fund is key” ... “and to continue managing the fund at moderate risk level”
- Secret placement agent payments scandal/internal audit – discussed – turmoil
- Tosh – CIO resigns - Brent Aldridge new interim CIO

**JUNE
BLACKSTONE/PRISMA KRS VISITS**

- June 9 Blackstone - meets KRS staff
- June 17 Prisma - meets KRS staff

**JULY 15/JULY 20
BUCHAN CALLS WITH TOSH AND ALDRIDGE**

- Aldridge has “little alternatives experience”
- “help him get up curve fast” –
- “perform our trusted advisor service to him”
- Told PAAMCO will be “1 of 3” to get absolute return/Fund of Funds Mandate

**JULY 21, 2010
LEGISLATIVE HEARING – RVK/VOYTKO**

- “while we are assuming 7.75% ... we know that’s not the real world”
- “impossible for pension plans to earn 7.75%”

**AUGUST 12
SPECIAL INVESTMENT COMMITTEE MEETING**

- Trustees Warned: hedge funds “Illiquid”
- Portfolio 1 – “more conservative” will earn **less** than 7.75%
- RVK recommends “more conservative”
- Portfolio 2 – “**more aggressive**” “**more aggressive**” “**more aggressive**” – will earn **over** 7.75%
- Trustees go aggressive
 - Trustee: “KRS members do not understand sophisticated market strategies” – “Won’t understand lower rate of return”
 - Trustee: “Portfolio 1 has lower rate of return” – will create “ANXIETY” among members
 - Trustee: “go with Portfolio 2 because of the higher projected returns” – will look “BETTER”

NEW ALLOCATION OF KRS TRUST FUNDS:

- **Absolute Return – 0% to 10%**
Black Boxes Fund of Hedge Funds – 100% increase – \$1.5 billion
t
- **Real Return – 0% to 10% Commodities/oil-gas/timber – 100% increase – \$1.5 billion**
t

CREATES AN

- **AAIRR – 7.93% – Higher than “impossible” 7.75%**

SELL INCOME-PRODUCING ASSETS – BUY \$BILLIONS BLACK BOXES/COMMODITIES
KRS TRUSTEES’ MORE AGGRESSIVE INVESTMENT ALLOCATIONS

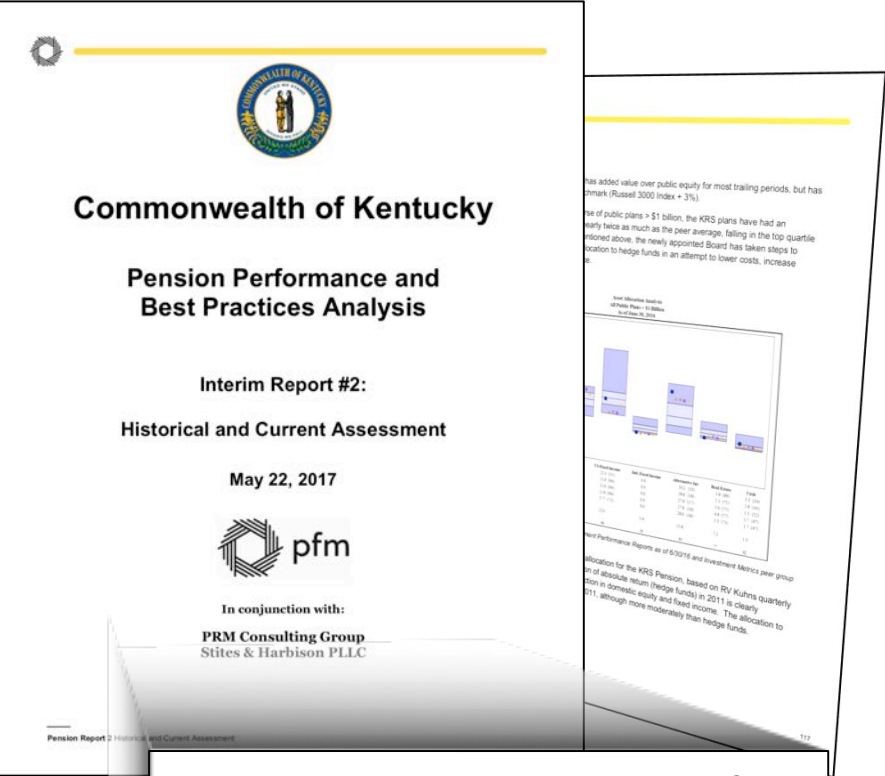
if they choose to pursue higher returns, they, of necessity, have to -- have to take on greater risks.
Voytko, 7/21/10 Transcript 24:9-21 Prisma #WW

AUGUST 12, 2010

Asset Class	Current Allocation	Potential Portfolio 2	Adopted 8/19/10	% Change Sold / Bought
Broad US Equity	27.2%	18.0%	20.0%	- 34%
Core Fixed Income	21.5%	10.0%	10.0%	- 53%
TIPS	10.4%	0.0%	0.0%	- 100%
Absolute Return	0.0%	10.0%	10.0%	+100%
Real Return	0.0%	10.0%	10.0%	+100%
Expected Return	7.62%	7.97%	7.93%	

BLACK BOX
FUND OF
HEDGE
FUNDS

COMMODITIES,
OIL, GAS,
ENERGY



The addition of absolute return hedge funds in 2011 ... clearly coincides with a reduction in domestic equity and fixed income.

7.62%

7.93%

TRUE RISKS OF THE “BLACK BOXES” BLACKSTONE/KKR 10-K SEC FILINGS

Our ordinary Hedge Funds:

- *newly established without any operating history or track records*
- *illiquid* investment vehicles
- invest in markets that are **volatile** – impossible to liquidate
- *could result in significant losses*
- *Use leverage – significant degree of risk – enhances possibility of significant loss subject to unlimited risk of loss in -- short selling, commodities*

OUR HEDGE FUNDS

- Involve **risk of loss** that investors ... should be prepared to bear high degree of business and financial risk that can result in **substantial loss**

AND THESE

RISKS EXACERBATED FOR OUR FUNDS OF HEDGE FUNDS

- Trustees bought – breached their Fiduciary Duties ¶233, 248
- Hedge Fund Sellers sold – breached their Fiduciary Duties ¶14,106, 231
- Trustees bought to justify 7.93% AAIRR – Gain time – Cover up – Gamble – **False Sense of Security** ¶7, 20, 137, 169, 215-243
- Hedge Fund Sellers sold to get hundreds of millions in fees – preyed on Trustees and aided and abetted the continued **False Sense of Security** ¶17, 104, 105, 239-243
- KRS Funds and Kentucky taxpayers paying price – nearly \$1 billion more/year in perpetuity ¶17,21-22, 30

The image shows two overlapping SEC Form 10-K filings. The top filing is for Blackstone, The Blackstone Group L.P., Commission File Number 001-33551. The bottom filing is for KKR & CO. L.P., Commission File Number 001-34820. Both filings are dated for the fiscal year ended December 31, 2016. The filings are titled "UNITED STATES SECURITIES AND EXCHANGE COMMISSION FORM 10-K" and "ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934".

HOW DID THE BLACK BOXES DO?
WORSE THAN CASH

ADDENDUM B – FUND OF HEDGE FUND MEMORANDUM – FEBRUARY 3, 2009

To: Investment Committee

From: KRS Investment Staff

Date: February 3, 2009

Subject: **KRS Absolute Return Strategy Allocation** **PCM #11**


Recommendation:

It is the recommendation of the KRS Investment Staff and Consultant that the Investment Committee approve an initial allocation of up to 5.0% of the Fund’s assets to be invested in absolute return strategy fund-of-funds (“FOF”).

ABSOLUTE RETURN
STRATEGY ALLOCATION



fund of fund implementation is designed to provide KRS with added active return ... will serve as a **long-term driver of performance** ... the expected long-term returns of many investment opportunities today have **tremendous potential to exceed the plan’s actuarial assumption.**

ABSOLUTE RETURNS  **PCM #14**

For the fiscal year, ending June 30, 2016, the KRS pension fund’s absolute return portfolio was -6.26%

3.73%

Return on Absolute Return

Portfolio	Inception Date	Fiscal Year	3-Year	5-Year	10-Year	Inception
Pension Fund	Apr-10*	-6.26%	2.36%	3.93%	--	3.73%

*Arrowhawk Hedge Fund Investment

CASH **3.75%**

Return on Cash

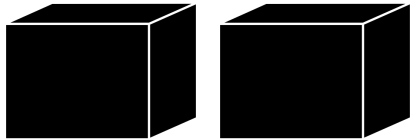
Portfolio	Inception
Pension Fund	Jan-88 3.75%



2015-16

\$1.5-\$1.8 Billion

“Black Boxes”

 **x 6.26% loss**

=

\$94-112 Million loss

SUBSCRIPTION AGREEMENTS – ULTIMATE *BAIT AND SWITCH*

- Dark of Day –
Bait/Switch
– send in your money
– forfeit your rights
- Duplicitous/Deceitful
– Fiduciary can't do this
to beneficiary
- Switched their legal duties of
protection/suitability on to
beneficiary
– law turned upside down
- This is an unlawful
course of business
– punitive damages

NEWPORT COLONELS, LLC

PAAMCO

SUBSCRIPTION AGREEMENT

I. (B) The investor has received
... **the LLC Agreement** ...
Investor acknowledges that in
making a decision to subscribe...
Investor has relied **solely**
upon the LLC Agreement
Investor ... adopts all
provisions contained in the
LLC Agreement.

DANIEL BOONE FUND, LLC

KKR
PRISMA

SUBSCRIPTION AGREEMENT

2. (B) Investor acknowledges in
making its decision ..., Investor
has relied **solely** upon the
Company Agreement.

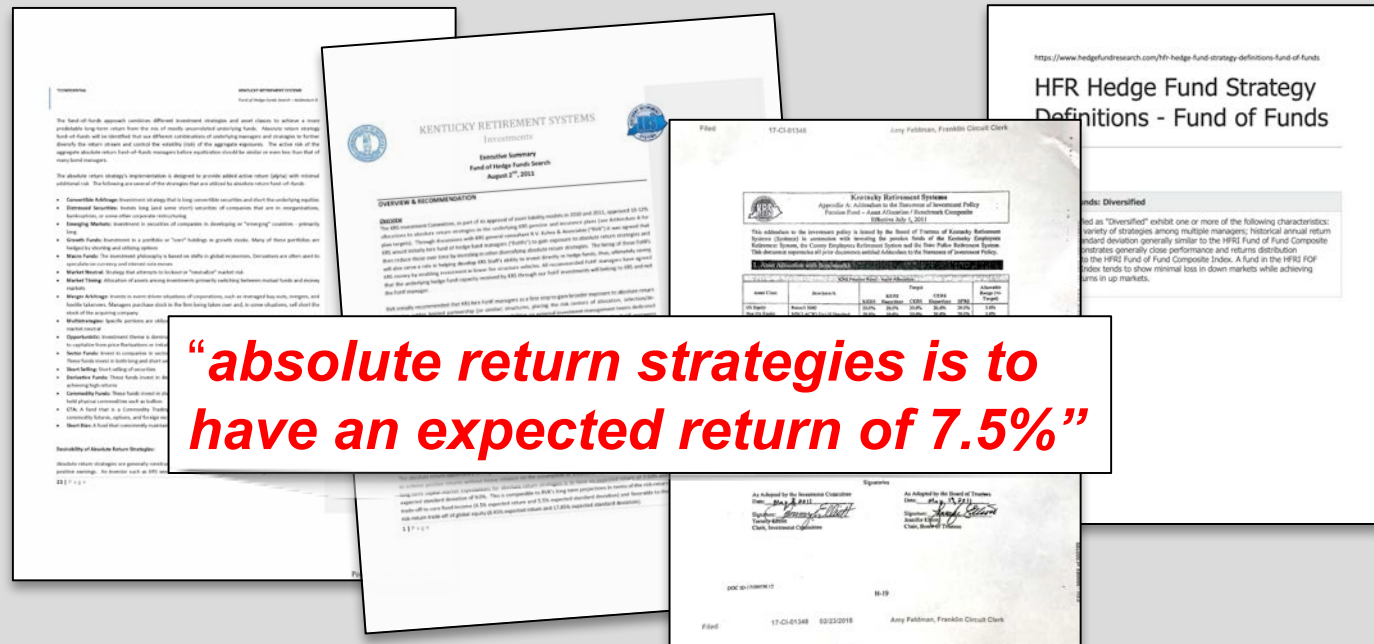
HENRY CLAY FUND, LLC

Blackstone

SUBSCRIPTION AGREEMENT

I. (B) The Investor acknowledges
... Investor has relied **solely**
upon the Company
Agreement

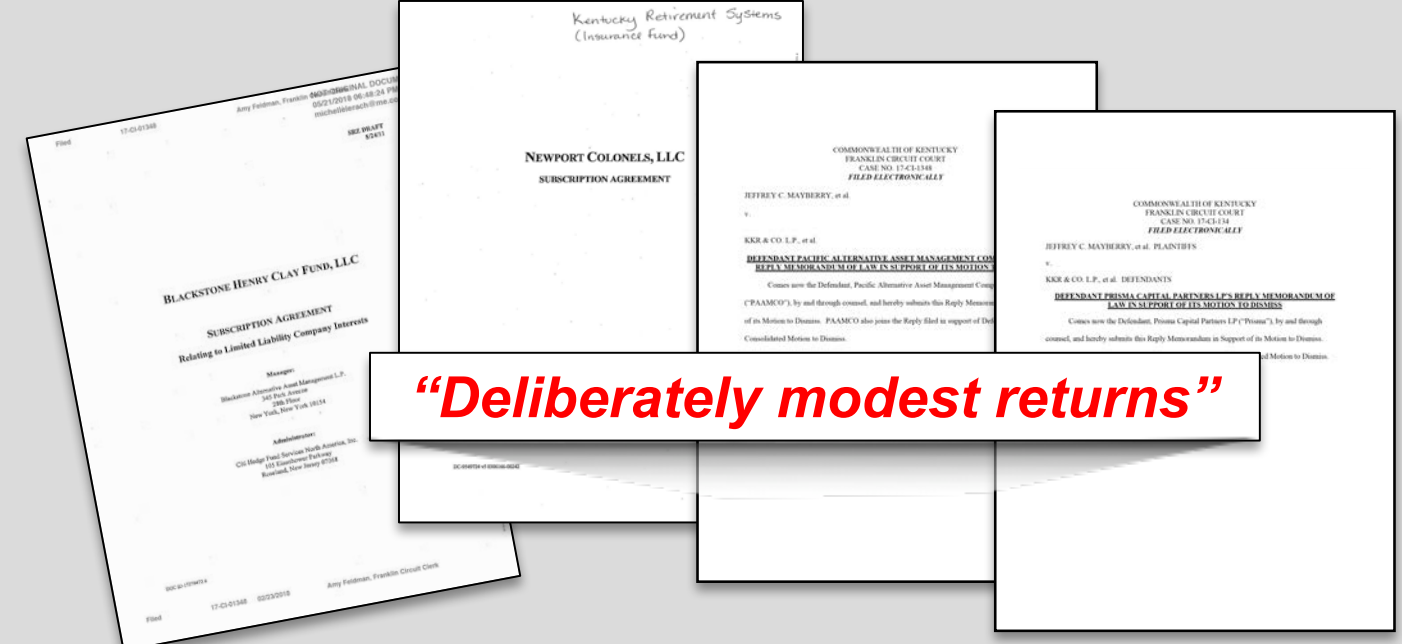
HEDGE FUND SELLERS – BAIT AND SWITCH



WHAT KRS EXPECTED EARLY AUGUST 2011

“Superior Returns” 7.5% per annum

- 2/3/09 “the expected returns ... of [absolute return FOFs] have **tremendous potential to exceed** the Plan’s **actuarial return assumptions**”
- 7/31/11 KRS adopts “HFR Diversified FOF” App. A to Statement of Investment Policy - defined by HFR as “**superior returns**”
- 8/2/11- KKR Executive summary FOHF Search: “**expected return of 7.5%**”



WHAT WAS SLIPPED INTO LLC WHAT THEY GOT

“Modest Returns” 3.3-5.3% per annum

- LLCs: 3-month LIBOR* + 300-500 basis points
- PAAMCO: “*absolute returns* strategies ... are designed to earn modest returns ...” and “3-month LIBOR rate ... was a deliberately modest return set by KRS.” Reply, at 1, 7.

*LIBOR on 8/26/11 = .32% according to Federal Reserve Bank, St. Louis

CONTRACTUAL DILUTION/AVOIDANCE OF FIDUCIARY/SUITABILITY DUTIES: FORBIDDEN UNDER FEDERAL & KENTUCKY LAW



Federal Law

1940 INVESTMENT ADVISORS ACT

Very purpose of 1940 Advisors Act was to prevent sophisticated money managers from doing just this – taking advantage of clients – shifting their duties under law to clients by slight of hand

- *it is hereby declared that the national public interest and the interest of investors are adversely affected ... when the business of investment advisers is so conducted ... to enable such advisers to relieve themselves of their fiduciary obligations to their clients.*
- *It is hereby declared that the policy and purposes of this title ... are to ... eliminate the abuses enumerated in this section.*

SEC v. Capital Gains Research Bureau, 375 US 180, 189 – 190 (1963)

Section 215 of the Advisors Act:

Validity of Contracts

(a) Waiver of compliance as void

Any condition, stipulation, or provision binding any person to waive compliance with any provision ... or with any rule, regulation, or order thereunder shall be void.

(b) Rights affected by invalidity

Every contract made in violation of any provision of **this subchapter ...the performance of which involves the violation of, ... of any relationship or practice in violation of any provision of this subchapter, or any rule, regulation, or order thereunder, *shall be void....***

- Plaintiffs **did not plead** LLC or Subscription Agreements
- Defendants are asserting LLC Agreements offensively to defend fiduciary duty claim
- Which is forbidden under Federal/Kentucky Law

SUPREME COURT

“By declaring certain contracts void, §215 by its terms necessarily contemplates the issue of voidness can be litigated somewhere. **At the very least Congress must assumed that §215 could be raised defensively in private litigation to preclude the enforcement of an investment advisers contract.**”

Transamerica Mortgage Advisors, v. Lewis, 444 U.S. 11, 18-19 (1979)

WHEN HFS PLEAD LLCs COURT WILL NEED TO ADDRESS THE ISSUE OF VALIDITY



Kentucky Law

HFS are Statutory and Common Law Fiduciaries --

- Kentucky Common Law. *Steelvest* – **can not take advantage** – ¶184,174 164
 - Breach of Fiduciary Duty by Trustees to Agree to Dilution of Obligations/Rights
 - Breach of Fiduciary Duty by HFS to impose self serving terms – on beneficiary

- KRS Investment Policy – Force of Law – *Agree to serve as fiduciary*

- Kentucky Securities Laws: investment adviser as defined by KRS 292.310(11) is a fiduciary pursuant to 808 KAR 10:450:

Section 2. [The] following shall be considered either a *breach of fiduciary duty or a dishonest and unethical practice.*

* * *

(19) Including in an advisory contract any condition, stipulation, or provision binding any client to waive compliance with any provision of the Securities Act of Kentucky, KRS Chapter 292, 808 Chapter 10 or of the Investment Advisors Act of 1940, 15 U.S.C. 80b.

FALSEHOODS - KRS ANNUAL REPORTS

ABSOLUTE RETURN - IMPROVED RETURNS - REDUCED RISK

TRUSTEES *Board's strategic decision to improve returns while reducing risk, new allocation to absolute return.*

RVK **Lower risk – Not illiquid – Will beat 7.75%**

adopted most effective asset allocation strategies to lower risk, control the level of illiquidity in the portfolios, and generate a return expected to exceed the actuarially assumed rate of return of 7.75%

return of 7.75%

... As of 2010 - 2011 ... the Board has been transitioning *transitioning ... in a prudent manner*

... We expect the Board's c
goals and objectives. ¶257

Board's continued high standard of care

System to meet its long-term

CAV MAC **Funding to increase to 100% – Adequate funding of liabilities**

the funding level ... should increase over time until it reaches 100%. ... adequate provisions are being determined for the funding of the actuarial liabilities ... as required by the Kentucky Revised Statutes. ¶263

Based on the ... current funding policies ... adequate provisions are being determined for the funding of the actuarial liabilities ... as required by the Kentucky Revised Statutes. ¶263

GFOA **Outstanding stewardship – Excellence satisfies legal requirements**








Because of the trustees outstanding stewardship

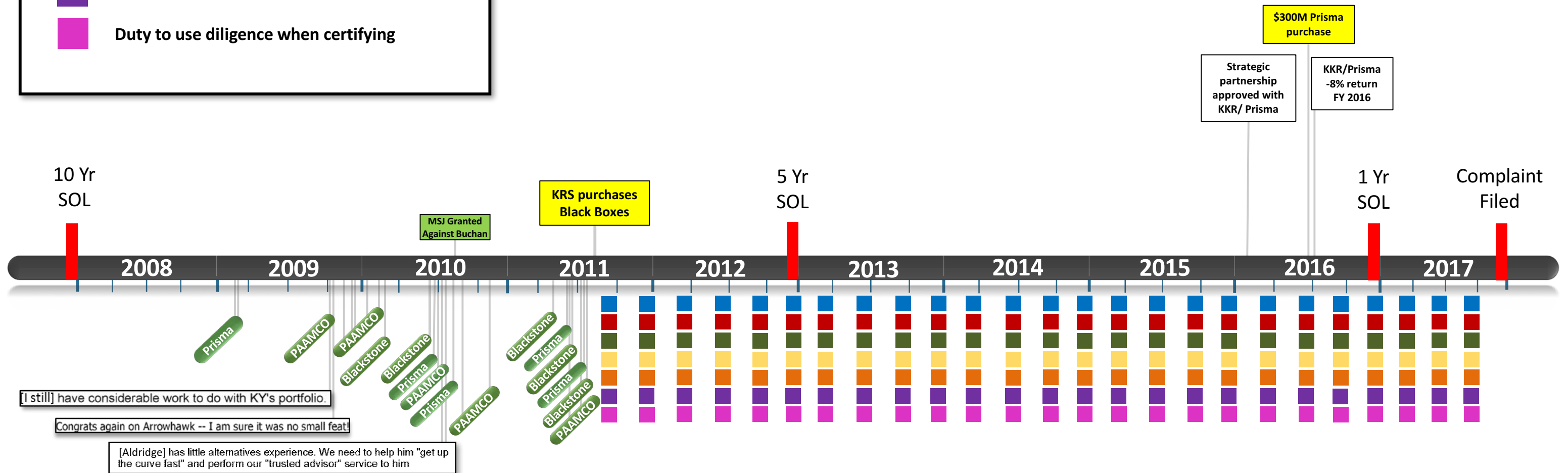
*Excellence in Preparation of its financial reports and
requirements. ¶264, 298*

Excellence in Preparation of its financial reports

Annual Report satisfies applicable legal requirements

Dates and Duties

-  Duty to monitor
-  Duty to remove imprudent investments
-  Duty to avoid excessive fees
-  Duty to use realistic actuarial assumptions
-  Duty to avoid conflicts
-  Duty to provide fiduciary counsel
-  Duty to use diligence when certifying



Fiduciary Duty