KNOX COUNTY RETIREMENT
AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT
TRUST FUNDS OF KNOX COUNTY, TENNESSEE

Knoxville, Tennessee

FINANCIAL STATEMENTS

December 31, 2012

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KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

TABLE OF CONTENTS

Page Number

INTRODUCTORY SECTION:

Roster of Board Members, Officials and Others ..... i-ii

FINANCIAL SECTION:

Independent Auditor's Report 1-2

Management Discussion and Analysis 3-6

Basic Financial Statements:

Statement of Plans Net Position 7

Statement of Changes in Plans Net Position 8

Notes to the Financial Statements 9-26

REQUIRED SUPPLEMENTARY INFORMATION SECTION:

Schedule of Employer Pension Funding Progress – Last Six Valuation Dates 27

Schedule of Employer Pension Contributions – Last Six Years 28

INTERNAL CONTROL AND COMPLIANCE SECTION:

Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards* 29-30

INTRODUCTORY SECTION

KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

ROSTER OF BOARD MEMBERS, OFFICIALS AND OTHERS

December 31, 2012

Board Members	**Expiration of Term**
Mr. Rick Trout, Chairman, Captain Knox County Sheriff's Department – Elected County Employee	February, 2015
Mr. Edward Shouse, Vice - Chairman, Knox County Commissioner – County Appointed	August, 2014
Mr. Nick McBride, Secretary Elected County Employee	February, 2017
Dr. Richard Briggs, Knox County Commissioner – County Appointed	August, 2014
Mr. Mike Hammond, Knox County Commissioner – County Appointed	August, 2014
Mr. Tony Norman, Knox County Commissioner – County Appointed	August, 2014
Mr. Chris Caldwell, MBA, Knox County Finance Director – Designee of the Knox County Mayor	August, 2014
Mr. Steve Glenn, Elected Knox County Schools	February, 2015
Mr. Joe Snyder, Elected Knox County Schools	February, 2017

Management

Ms. Kim Bennett, Executive Director

Ms. Della Ledford, Assistant Executive Director

Ms. Jennifer Schroeder, Financial Retirement Manager

Ms. Janet Rowan, Retirement Benefit Manager

Independent Auditors

Pugh & Company, P.C.
Certified Public Accountants
Knoxville, Tennessee

Actuary and Third Party Administrator

Mr. Bob Cross, ASA, MAAA, FCA
USI Consulting Group
Knoxville, Tennessee

KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

ROSTER OF BOARD MEMBERS, OFFICIALS AND OTHERS (Continued)

December 31, 2012

Legal Counsel

Mr. Richard Beeler, General Counsel
Robertson, Overby, Wilson & Beeler
Knoxville, Tennessee

Mr. William Mason, Special Counsel
Kennerly, Montgomery & Finley
Knoxville, Tennessee

Investment Trustees and Custodians

State Street Bank & Trust Company
Boston, Massachusetts

Wells Fargo Bank
Charlotte, North Carolina

Investment Consultants

Wilshire & Associates
Pittsburgh, Pennsylvania

USI Advisors
Glastonbury, Connecticut

Investment Managers

State Street Global Advisors
Boston, Massachusetts

T. Rowe Price
Baltimore, Maryland

Capital Guardian
New York, New York

Pyramis International
Smithfield, Rhode Island

Schroder Investment Management
New York, New York

Chicago Equity Partners
Chicago, Illinois

Loomis Sayles
Boston, Massachusetts

Adelante Capital Management
Oakland, California

Prudential Life Insurance Company
Parsippany, New Jersey

Brown Brothers Harriman
New York, New York

FINANCIAL SECTION

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PUGH & COMPANY, P.C.
www.pughcpas.com

INDEPENDENT AUDITOR'S REPORT

Members of the Knox County
Retirement and Pension Board
Knoxville, Tennessee

Report on the Financial Statements

We have audited the accompanying financial statements of the Knox County Retirement and Pension Board and System (the "System"), pension, retirement and employee benefit trust funds of Knox County, Tennessee, which comprise the statement of plans net position as of December 31, 2012 , and the related statement of changes in plans net position and related notes to the financial statements for the year ended December 31, 2012.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Basis for Qualified Opinion

Because we did not perform auditing procedures with respect to the System's Defined Contribution Plan's individual participant account balances accumulated from inception, we were unable to satisfy ourselves as to the basis on which participants' equity is stated as of the beginning and end of the year ended December 31, 2012, or the proprietary of the benefits paid to participants during the year then ended. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.

Qualified Opinion

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the System as of December 31, 2012 and the changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2, the financial statements of the Knox County Retirement and Pension Board and System are intended to present only the statements of plan net position and changes in net plan position of the System. They do not purport to, and do not, present fairly the financial position of Knox County, Tennessee, as of December 31, 2012, and the changes in its financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters - Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management Discussion and Analysis on pages 3 through 6 and the Schedules of Employer Pension Funding Progress and Employer Pension Contributions on pages 27 and 28 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The introductory section is presented for purposes of additional analysis and is not a required part of the financial statements.

The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated August 23, 2013, on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control over financial reporting and compliance.

Pugh & Company, P.C.

Certified Public Accountants
Knoxville, Tennessee
August 23, 2013

KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

MANAGEMENT DISCUSSION AND ANALYSIS

December 31, 2012

The accompanying financial statements of the Knox County Retirement and Pension Board and System ("the Retirement Board" and "System") reflect the Defined Benefit ("DB Plans") and Defined Contribution ("DC Plans") Plans' investment of assets, the payments of benefits and the operational costs for the year ended December 31, 2012. The measurement focus is to show the value and annual change in the plans net position restricted for pension and retirement benefits for the employees and participants. The accounting statements are prepared on an accrual basis and are in accordance with the Government Accounting Standards Board (GASB) pronouncements. The Plans are managed by the Knox County Retirement & Pension Board (the Board) and its executive director.

The Plans cover eligible employees of Knox County, Tennessee ("County"), Knox County Board of Education ("BOE") and certain affiliated entities.

Financial Highlights

The System's net position restricted for pension and retirement benefits as of December 31, 2012 is $479 million. The total Plans net position are available to meet the System's ongoing obligations to current Knox County and BOE employees, plan participants and their beneficiaries.

The System's net position increased $47.5 million, or 11%, during 2012 due mainly to improved financial markets. For 2012 total investment income was $53.6 million, contributions were $29.1 million and benefits paid were $33.8 million.

The System's total net investment income for 2012 was $53.6 million as compared to a net investment loss of $2.8 million for 2011. The total Plans overall investment return for 2012 was 12.5% which was above the long term assumed rate of 7.0% for the Defined Benefit Plans.

Additions to total net plan position during 2012 included employer contributions of $17.5 million, employee contributions of $11.3 million and employee rollover contributions of $285,249 for a total of $29.1 million as compared to 2011 total contributions of $26.8 million.

Deductions from total net plan position for 2012 were $35.4 million, a decrease of $2.3 million due to a decrease in benefits paid in the current year of $1.8 million. Administrative expenses decreased from $1.8 million in the prior year to $1.4 million in 2012.

The System's DB Plans overall funding ratio increased during 2012. The funded ratio is calculated as the ratio of the market value of assets to the present value of accumulated benefits, as of the actuarial valuation date (January 1) of each respective Plan year. The funded ratio for each of the System's DB Plans as of January 1, 2013 and 2012 is as follows:

	2012	2011
Closed Defined Benefit Plan	69.6%	68.2%
Teachers Plan	82.1%	79.1%
UOPP	98.8%	84.4%

GASB also requires computation of a funding ratio determined as the ratio of the actuarial value of Plan assets to the actuarial accrued liability determined utilizing the individual entry age normal funding method. The applicable ratios are provided in the Required Supplementary Information Section of this report.

The System's major DB actuarial assumptions included a decrease in the long term assumed rate of return of investments, or the discount rate, from 7.5% in 2011 to 7.0% for 2012. In addition, the projected salary increases were lowered from 3.5% to 3.0% during 2012.

Overview of the Financial Statements

The following discussion and analysis is intended to serve as an introduction to the System's financial statements which follow. The financial statements report information about the System using full accrual accounting methods, and reporting investments at fair value as required by the GASB and include the following:

Management Discussion and Analysis
Statement of Plans Net Position
Statement of Changes in Plans Net Position
Notes to the Financial Statements
Required Supplementary Information
Internal Control and Compliance Section

Management's Discussion and Analysis (MD&A) serves as the introduction to the basic financial statements and represents management's analysis of the System's financial condition and performance. Summary financial data and other key indicators used in the System's operations of the Plans and other management information were used for this analysis.

The Statement of Plans Net Position is a snapshot of account balances at year-end. It indicates the assets available for future payments to retirees and any current liabilities.

The Statement of Changes in Plans Net Position shows the additions and deductions from the System's assets over the current year.

Notes to the financial statements provide additional information which is essential for a full understanding of the data provided in the basic financial statements.

Required Supplementary Information provides additional information and details about the System's progress in funding its future obligations and the history of employer contributions to the defined benefit plans.

The Internal Control and Compliance Section includes the independent auditor's report on the System's internal controls and compliance in accordance with *Government Auditing Standards*.

Financial Analysis

The following comparative condensed financial statements and other selected information provide key financial data and indictors for management, monitoring, and planning. The tables below provide a summary of the System's financial condition and results for the current and prior year for comparative purposes.

At the close of the 2012 year, the System's assets exceeded liabilities by $479,725,124. The following table provides a summary of the System's net position as of December 31, 2012 and 2011.

	($ in thousands) As of December 31,	
Statements of System's Net Position	2012	(Restated) 2011
Assets		
Cash and Cash Equivalents	$ 3,711	$ 4,646
Investments	474,679	426,904
Receivables	1,487	878
Prepaid Expenses	0	10
Total Assets	479,877	432,438
Liabilities		
Accounts Payable	(152)	(280)
System's Net Position - Restricted	$ 479,725	$ 432,158

Financial Analysis (Continued)

The following table provides a summary of the changes in net position for the years ended December 31, 2012 and 2011.

Statements of Changes in System's Net Position	($ in thousands) For the Years Ended December 31, 2012	(Restated) 2011
Additions		
Net Investment Income (Loss)	$ 53,577	$ (2,776)
Participant Contributions	11,355	11,258
Employer Contributions	17,504	15,149
Rollover Contributions	285	402
Transfers In	293	281
Total Additions	83,014	24,314
Deductions		
Benefits Paid	33,797	35,561
Administrative Expenses	1,357	1,835
Transfers Out	293	281
Total Deductions	35,447	37,677
Increase (Decrease) in System's Net Position	$ 47,567	$ (13,363)

Analysis of Additions and Deductions from the Plans

Employer contributions increased by $2,355,414 during 2012 of which $1,993,055 was for the DB plans. Knox County increased its employer contributions to the Closed Defined Benefit Plan by $1,535,171 and the UOPP by $395,510 for 2012 when compared to 2011. The increases in DB employer contributions were due to increases as recommended by the System's actuary. The DC employer matching contribution percentages did not change during 2012.

Net investment income was $53.6 million for 2012 when compared to a loss of $2.8 million for 2011. The System's net investment yield was 12.5% for 2012 as compared to a loss of .63% for 2011. During 2012 the financial markets experienced significant improvement in equities with smaller increases in bonds when compared to 2011 as indicated by the following market indices:

Index (Includes Dividends & Interest)	2012	2011
S&P 500	15.9 %	2.1 %
Russell U.S. Midcap	17.3 %	-1.4 %
MSCI All-World Equity	16.6 %	-5.5 %
Barclays Intermediate Government Bond	3.9 %	6.1 %
Barclays U.S. Aggregate Bond	4.2 %	7.9 %

Total benefits paid by the System decreased by $1.8 million during 2012. When compared to the prior year, the DB Plans increased benefits paid by $1.0 million due to a 3% cost of living adjustment (COLA) and a slight increase in the number of retirees and the DC Plans decreased benefits paid by $2.8 million in the current year.

The System’s total administrative expenses, which are allocated only to the DB Plans, decreased from $1.8 million in 2011 to $1.4 million in 2012, a net decline of $478,029. The 2012 decrease is a result of the System’s staffing reduction by 1 & ½ positions and less occupancy and overhead costs charged to the Plans by Knox County.

Future Outlook for 2013

The Retirement Board anticipates that the County and BOE will increase the 2013 employer contributions to fund the liabilities of the DB Plans. The recommended actuarial employer contributions from Knox County and BOE for the DB Plans during 2013 will be approximately $8.7 million which is $500,000 or 6% greater than the recommended contributions for 2012.

The System is currently in the process of developing a new defined contribution plan for the Knox Sherriff's Department Officers to replace the UOPP defined benefit plan as was approved by the Knox County voters in a November 2012 referendum. In addition, the Retirement Board is developing a new disability plan to cover Knox County and Board of Education employees. The Disability Plan will be funded and reported under Other Post Employment Benefit (OPEB) rules and will provide disability benefits to participants who are disabled on and after January 1, 2014, instead of disability benefits coverage currently provided under the closed defined benefit and UOPP.

Requests for Information

This financial report is designed to provide a general overview of the Systems DB and DC Plans' finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Ms. Kim Bennett, Executive Director, Knox County Retirement and Pension Board, City-County Building, Room 371, 400 Main Street, Knoxville, Tennessee 37902-2409.

KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

STATEMENT OF PLANS NET POSITION

December 31, 2012

	Defined Benefit Plans				Defined Contribution Plans				
	Closed Defined Benefit Plan	Teacher's Plan	Uniformed Officers Pension Plan	Total Defined Benefit Plans	Asset Accumulation Plan	Voluntary 457 Plan	Medical Expense Retirement Plan	Total Defined Contribution Plans	Total
ASSETS									
Cash and Cash Equivalents	$ 901,641	$ 1,130,691	$ 1,678,129	$ 3,710,461	$ 0	$ 0	$ 0	$ 0	$ 3,710,461
Investments, at Fair Value									
Mutual Funds	44,313,248	55,586,071	105,507,211	205,406,530	174,437,930	7,456,201	3,358,236	185,252,367	390,658,897
Guaranteed Investment Contract	0	0	0	0	24,988,875	716,337	0	25,705,212	25,705,212
Common Collective Trusts	0	0	0	0	26,556,771	1,086,117	2,100,158	29,743,046	29,743,046
Corporate Bonds	592,434	743,144	1,335,018	2,670,596	0	0	0	0	2,670,596
U.S. Treasuries	2,427,897	3,045,528	5,691,906	11,165,331	0	0	0	0	11,165,331
Federal Agency Debt Securities	922,356	1,156,989	2,675,795	4,755,140	0	0	0	0	4,755,140
Federal Agency Mortgage Backed Securities	1,993,453	2,500,566	5,487,193	9,981,212	0	0	0	0	9,981,212
Total Investments	50,249,388	63,032,298	120,697,123	233,978,809	225,983,576	9,258,655	5,458,394	240,700,625	474,679,434
Receivables									
Participant's Contributions	655	0	0	655	19,410	693	446	20,549	21,204
Employer Contributions	0	0	0	0	19,410	0	90	19,500	19,500
Accrued Interest and Dividends	41,850	52,618	102,102	196,570	0	0	0	0	196,570
Receivable for Investments Sold	553,750	696,250	0	1,250,000	0	0	0	0	1,250,000
Total Receivables	596,255	748,868	102,102	1,447,225	38,820	693	536	40,049	1,487,274
Prepaid Expenses	0	0	0	0	0	0	0	0	0
Total Assets	51,747,283	64,911,857	122,477,354	239,136,494	226,022,396	9,259,348	5,458,930	240,740,674	479,877,168
LIABILITIES									
Accounts Payable - Administrative Expenses	(35,188)	(59,139)	(57,717)	(152,044)	0	0	0	0	(152,044)
NET POSITION - RESTRICTED FOR PENSION AND RETIREMENT BENEFITS	$ 51,712,095	$ 64,852,718	$ 122,419,637	$ 238,984,450	$ 226,022,396	$ 9,259,348	$ 5,458,930	$ 240,740,674	$ 479,725,124

(A Schedule of Funding Progress for Defined Benefit Plans is presented in the Required Supplementary Section of this report.)

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

KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

STATEMENT OF CHANGES IN PLANS NET POSITION

For the Year Ended December 31, 2012

	Defined Benefit Plans				Defined Contribution Plans				
	Closed Defined Benefit Plan	Teacher's Plan	Uniformed Officers Pension Plan	Total Defined Benefit Plans	Asset Accumulation Plan	Voluntary 457 Plan	Medical Expense Retirement Plan	Total Defined Contribution Plans	Total
ADDITIONS									
Investment Income (Loss)									
Net Appreciation (Depreciation) in Fair Value of Investments	$ 7,183,725	$ 9,010,199	$ 14,777,089	$ 30,971,013	$ 17,986,957	$ 780,349	$ 178,732	$ 18,946,038	$ 49,917,051
Interest and Dividends	349,815	441,287	804,978	1,596,080	2,952,239	112,406	54,052	3,118,697	4,714,777
Less: Investment Expense	(275,482)	(341,648)	(437,713)	(1,054,843)	0	0	0	0	(1,054,843)
Net Investment Income (Loss)	7,258,058	9,109,838	15,144,354	31,512,250	20,939,196	892,755	232,784	22,064,735	53,576,985
Contributions									
Participant's	168,472	32,549	1,700,212	1,901,233	7,708,533	1,527,434	217,376	9,453,343	11,354,576
Employer	2,870,544	1,183,029	4,709,512	8,763,085	8,689,379	0	51,832	8,741,211	17,504,296
Rollovers	0	0	0	0	260,366	24,883	0	285,249	285,249
Total Contributions	3,039,016	1,215,578	6,409,724	10,664,318	16,658,278	1,552,317	269,208	18,479,803	29,144,121
Other									
Transfers In from Other Plans	0	0	0	0	74,884	0	218,000	292,884	292,884
Total Additions	10,297,074	10,325,416	21,554,078	42,176,568	37,672,358	2,445,072	719,992	40,837,422	83,013,990
DEDUCTIONS									
Benefits Paid to Participants	7,598,919	6,463,183	3,496,227	17,558,329	15,014,189	456,603	767,354	16,238,146	33,796,475
Administrative Expenses	367,883	338,632	650,867	1,357,382	0	0	0	0	1,357,382
Transfers to Other Plans	292,884	0	0	292,884	0	0	0	0	292,884
Total Deductions	8,259,686	6,801,815	4,147,094	19,208,595	15,014,189	456,603	767,354	16,238,146	35,446,741
NET INCREASE (DECREASE) IN NET POSITION	2,037,388	3,523,601	17,406,984	22,967,973	22,658,169	1,988,469	(47,362)	24,599,276	47,567,249
NET POSITION - RESTRICTED FOR PENSION AND RETIREMENT BENEFITS, BEGINNING OF YEAR (Restated for Defined Contribution Plans, See Note 11)	49,674,707	61,329,117	105,012,653	216,016,477	203,364,227	7,270,879	5,506,292	216,141,398	432,157,875
NET POSITION - RESTRICTED FOR PENSION AND RETIREMENT BENEFITS, END OF YEAR	$ 51,712,095	$ 64,852,718	$ 122,419,637	$ 238,984,450	$ 226,022,396	$ 9,259,348	$ 5,458,930	$ 240,740,674	$ 479,725,124

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

KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

NOTES TO THE FINANCIAL STATEMENT

December 31, 2012

NOTE 1 - DESCRIPTION OF THE KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM AND PLANS

Administration - The Knox County Retirement and Pension Board and System ("Retirement Board" and "System") was created by Tennessee General Assembly, House Bill No. 866, Chapter 246, Private Acts 1967-68, as amended. The powers of the Retirement Board are governed by the Knox County Charter, Article VII, as amended. The Retirement Board is governed by nine members who include the (a) County Mayor, or his designee, (b) four members of the Knox County Commission and (c) four current employees of Knox County Government and Board of Education who are participating members of the System and elected by the current employees. Elected Board members serve staggered four year terms and the County Mayor and four County Commission members serve concurrently with their terms as elected County Officials.

The Retirement Board employs an executive director who is responsible for administering the pension and retirement plans. The Board has appointed State Street Bank & Trust Company and Wells Fargo Bank as investment trustees and custodians who handle accounting for financial transactions and distributions to the Plans participants. In addition, the System uses USI Consulting Group, Inc. as the actuary for its defined benefit plans and as third party administrator to help in administering the defined contribution plans. The Retirement Board has also hired several different investment advisors to manage its investment portfolio for its defined benefit plans.

The following brief descriptions of the System's Plans are provided for general information only. Participants should refer to the various Plan documents for more complete information.

Employee Retirement and Income Security Act of 1974 (ERISA) - According to the Employee Retirement Income Security Act of 1974 (ERISA), the System operates governmental pension and retirement plans and is not subject to the statutory provisions of ERISA.

Eligibility - The System covers employees of Knox County Government, Knox County Board of Education classified education employees (not certified), the Knoxville-Knox County Public Building Authority, and various other related entities. Employees (participants) can become participants immediately upon employment and must be scheduled to work a minimum of 18.5 hours or more per week to be eligible to enroll and continue to participate in the various Plans.

Plans - The System operates six single-employer pension and retirement plans which consist of defined benefit and defined contribution plans and include the following:

> **Defined Benefit Plans:** This includes the Closed Defined Benefit Plan (closed to new participants as of September 30, 1991), Teacher's Plan (assumed from the former City of Knoxville Board of Education July 1, 1987 and closed to new participants as of July 1, 1977) and the Uniformed Officers Pension Plan (UOPP which is scheduled to be closed to new Sheriff's Department Officers employed on or after January 1, 2014).
>
> **Defined Contribution Plans:** This includes the Asset Accumulation Plan, Voluntary 457 Plan and the Medical Expense Retirement Plan (MERP). The Asset Accumulation Plan is mandatory for all eligible employees hired after October 1, 1991 who are not covered by UOPP or the Tennessee Consolidated Retirement System (TCRS).

NOTE 1 - DESCRIPTION OF THE KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM AND PLANS (Continued)

Plan Termination - No provision has been made for the System's termination and resulting order of allocation of benefits if termination should occur. The Pension Benefit Guaranty Corporation (PBGC), a U.S. Government backed insurance program, does not insure the System's defined benefit plans.

Plan Membership - As of December 31, 2012, the System had the following membership for all pension and retirement plans:

	Defined Benefit Plans			Defined Contribution Plans		
	Closed Defined Benefit Plan	Teacher's Plan	UOPP	Asset Accumulation Plan	Voluntary 457 Plan	Medical Expense Retirement Plan
Retirees and Beneficiaries Currently Receiving Benefits	941	451	76	917	90	2,087
Terminated Participants Entitled to, but not yet Receiving Benefits	263	8	14	353	N/A	N/A
Current Active Participants	103	7	739	4,341	657	653
Total	1,307	466	829	5,611	747	2,740

Contributions (Defined Benefit Plans) - The System operates three different single-employer defined benefit plans which are contributory plans that require the employer (Knox County and the Knox County Board of Education) to make contributions determined by annual actuarial valuations. In addition, participants are required to make employee contributions of varying percentages.

Contributions (Defined Contribution Plans) - Participants contributions of 6% to the Asset Accumulation Plan are mandatory and employees may voluntarily make qualified retirement contributions to the Voluntary 457 and MERP defined contribution Plans. Employee contributions are deducted pre-tax from the participants on a pay period basis for federal income tax purposes under Section 401(a) and 457(b) of the Internal Revenue Code. Participants may also rollover amounts representing distributions from other qualified defined benefit or defined contribution plans. Participants may elect to make tax-deferred contributions to the 457 Plan subject to annual IRS limitations. For the Voluntary 457 and MERP Plans, participants may change their contribution percentage monthly and participants may stop deferring with any payroll.

The Asset Accumulation and Voluntary 457 defined contribution plans allows participants to direct employee and employer contributions in a variety of mutual funds, common collective trusts and guaranteed investment contracts. Participants may change their investment options at their discretion. For the MERP the Retirement Board has selected one investment "mix" option for participants. The one MERP investment option consists of 25% fixed, 38% conservative and 37% moderate investment styles. The contributions for each participant are accounted for separately as to employer and participant contributions.

Participant Accounts (Defined Contribution Plans) - Each participant's account is credited with the participant's contribution, the employer's contributions and an allocation of plan earnings. The benefit to which a participant is entitled is the benefit which can be provided from the participant's vested account.

Participant Loans (Defined Contribution Plans) - Participant loans are not permitted.

Administrative Fees and Operating Expenses (Defined Benefit Plans) - Administrative fees include those charged by the investment custodians, advisors and third-party administrator. Operating expenses of the Knox County Retirement & Pension Board office are allocated to the Closed Defined Benefit Plan, Teacher's Plan and the Uniformed Officers Pension Plan. For the year ended December 31, 2012, administrative fees include $1,357,382 of operating expenses allocated to the Plans.

Forfeitures (Defined Contribution Plans) - Forfeitures of $479,909 were used to offset employer contributions to the Asset Accumulation Plan for the year ended December 31, 2012.

NOTE 1 - DESCRIPTION OF THE KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM AND PLANS (Continued)

Description of Defined Benefit Plans

	Closed Defined Benefit Plan	Teacher's Plan	UOPP
Effective and Closed Dates:	Plan was established July 1, 1968 and was closed to new participants on September 30, 1991.	Plan was previously a City of Knoxville Board of Education which was assumed by Knox County as of July 1, 1987.	Plan was established July 1, 2007 and is to be closed to new participants on December 31, 2013.
Employees Covered:	Employees of Knox County and the Knox County Board of Education (non-teachers) who were hired before the plan was closed on September 30, 1991 and did not choose to convert to the Asset Accumulation Plan.	Former City of Knoxville Board of Education teachers who were in the Plan as of June 30,1987 and regularly employed by the Knox County Board of Education.	Officers regularly employed by the Knox County Sheriff's Office and who do not participate in the Closed Defined Benefit or Asset Accumulation Plans.
Employees Excluded:	Employees of Knox County who participate in one of the other two defined benefit plans, or who participate in the Asset Accumulation Plan. Also Knox County Board of Education teachers and administrators who are participants in the Tennessee Consolidated Retirement System (TCRS).	Employees of Knox County who participate in one of the other two defined benefit plans, or who participate in the Asset Accumulation Plan. Also, Knox County Board of Education teachers and administrators who are participants in the Tennessee Consolidated Retirement System (TCRS).	Employees of Knox County who participate in closed DB Plans or who participate in the Asset Accumulation Plan.
Employee Contributions:	5% of Annual Compensation	3% of base earnings ($4,800 annually) with 5% for amounts in excess of base earnings.	6% of annual compensation, no employee contributions after a participant has completed 30 years of credited service.
Vesting:	100% after completing five years of credited service.	100% after completing ten years of credited service.	100% after completing five years of credited service.
Normal Retirement Age & Required Creditable Service:	Age 65, with five years of credited service. For elected official's, age 55 with five years of credited service.	Age 62, with ten years of credited service.	Age 50, with 25 years of credited service.
Normal Retirement Benefit Formula:	Years of credited service times the greater of (a) 1.75% of average monthly compensation or, (b) $30.	One-twelfth of credited service multiplied by the sum of (a) .75% times average base earnings and (b) 1.50% times average excess earnings.	Monthly benefit equal to 2.5% of average monthly compensation multiplied by years of credited service up to 30 years.
Normal Form of Benefit:	Life Annuity	Life Annuity	Life annuity for un-married participants. A 50% joint and survivor annuity for married participants.

(Table Continued On Next Page)

NOTE 1 - DESCRIPTION OF THE KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM AND PLANS (Continued)

Description of Defined Benefit Plans (Continued)

	Closed Defined Benefit Plan	Teacher's Plan	UOPP
Cost of Living Adjustments (COLA):	3% COLA of original monthly benefit one calendar year from retirement and continuing annually.	< Age 62 = 3% > Age 62 = 3% + 1/2 of CPI > 3% up to a maximum of 1% added.	< Age 62 = 3% > Age 62 = 3% + 1/2 of CPI > 3% up to a maximum of 1% added.
Average Monthly Compensation:	Monthly average of total compensation for the 60 consecutive months of the highest compensation prior to retirement.	Annual average of total compensation for three calendar years of the highest earnings prior to retirement.	Monthly compensation over any two 12 month periods of the highest earnings, including periods prior to the Plan's effective date.
Credited Service:	All continuous uninterrupted service expressed in years based upon completed calendar months.	Completed calendar months of service as an employee of either the City of Knoxville or Knox County Board of Education.	Completed calendar months of service as an employed Officer.
Early Retirement Benefit:	Age 55, with five years of credited service and benefits reduced by 0.4167% for each month that early retirement precedes normal retirement.	Age 50, with 25 years of credited service.	Completion of 25 years of credited service with benefits equal to 2.0% of average monthly compensation multiplied by years of credited service not to exceed 25 years.
Deferred Retirement Benefits:	None	None	2.0% of average monthly compensation multiplied by the participant's projected service (maximum 25 years), multiplied by actual years of service and divided by projected service.
Disability Benefit:	No minimum age. For disability not in the line of duty, five years of credited service; for disability in the line of duty, no minimum required service. Benefits are calculated as a monthly annuity payable to age 65 equal to 50% (60% if one dependent child) of average monthly compensation reduced by the participant's social security SSI or worker's compensation monthly benefits or other earned income.	Completion of 15 years of credited service. Benefits are payable immediately in a lump-sum equal to six times the accrued monthly benefit.	In the line of duty, 50% of average monthly compensation. Not in the line of duty, 2% x years of service x average compensation.
Death Benefits:	Lump sum equal to $300 multiplied by years of service up to 30 years.	None	A participant's surviving spouse receives 50% of the normal retirement benefits.

NOTE 1 - DESCRIPTION OF THE KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM AND PLANS (Continued)

Description of Defined Contribution Plans

	Asset Accumulation Plan	Voluntary 457 Plan	Medical Expense Retirement Plan
Eligibility and Participation:	Employees of Knox County and the Knox County Board of Education (non-teachers) who were hired after the Defined Benefit Plan was closed on September 30, 1991. Former participants of the Closed Defined Plan had the option to transfer to the Asset Accumulation Plan.	Employees of Knox County and the Knox County Board of Education (non-teachers) who are participating in the Asset Accumulation or the Closed Defined Benefit Plans.	Employees of Knox County and the Knox County Board of Education (non-teachers) who are participating in the Asset Accumulation or the Closed Defined Benefit Plans.
Employees Excluded:	Employees of Knox County who participate in one of the other three defined benefit plans. Certified teachers and administrators of the Knox County Board of Education covered by TCRS.	Employees of Knox County who participate in the Teachers and UOPP Plans, Certified teachers and administrators of the Knox County Board of Education covered by TCRS.	Employees of Knox County who participate in the Teachers and UOPP Plans, Certified teachers and administrators of the Knox County Board of Education covered by TCRS.
Employee Contributions:	6% of Annual Compensation (Mandatory)	Voluntary	Voluntary
Employer Matching Contributions:	6% of Annual Compensation	Less than five years of service 0%, more than five but less than 10 up to 2%, more than 10 but less than 15 up to 4%, and more than 15 years up to 6%. Closed DB participants are up to 3%. Matching employer contributions are credited to the participant's Asset Accumulation Plan account.	25% of employee contributions up to annual maximum of $104.
Vesting of Employer Matching Contributions	20% per year after completing one year of service with 100% after completing five years of credited service.	Immediate 100% vesting.	Immediate 100% vesting.
Normal Retirement Age & Required Creditable Service:	Age 65, with five years of credited service.	Age 65, with five years of credited service.	Age 59 & 1/2.
Normal Form of Benefit:	Life annuity with survivor benefits, fixed payment installments if less than 10 years life expectancy, and a modified 25% lump-sum distribution with either a life annuity or installment method.	Life annuity with survivor benefits, fixed payment installments if less than 10 years life expectancy, and a modified 25% lump-sum distribution with either a life annuity or installment method.	N/A

(Table Continued On Next Page)

NOTE 1 - DESCRIPTION OF THE KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM AND PLANS (Continued)

Description of Defined Contribution Plans (Continued)

	Asset Accumulation Plan	Voluntary 457 Plan	Medical Expense Retirement Plan
Credited Service:	All continuous uninterrupted service expressed in years based upon completed calendar months.	N/A	All continuous uninterrupted service expressed in years based upon completed calendar months.
Early Retirement Benefit:	Age 55, with five years of credited service.	N/A	N/A
Disability Benefit:	No minimum age with five years of credited service. Benefits are 50% of (60% if one dependent child) your average earnings based upon the highest five year preceding disability payable until age 65. Benefits are reduced by the participant's social security SSI or worker's compensation benefits or other earned income.	N/A	N/A
Termination of Employment:	Less than five years of service and vested account balance is $5,000 or less, immediate lump-sum distribution. If five years of service and vested account balance is $5,000 or less, option of lump-sum distribution or rollover. If five years of service and vested balance is more than $5,000, option of lump-sum, rollover or leave amount in the Plan.	Less than five years of service and vested account balance is $5,000 or less, immediate lump-sum distribution. If five years of service and vested account balance is $5,000 or less, option of lump-sum distribution or leave amount in the Plan. If five years of service and vested balance is more than $5,000, option of lump-sum, rollover or leave amount in the Plan.	If account balance is less than $5,000, immediate lump-sum distribution. If account balance is more than $5,000, lump-sum, rollover to another qualified plan, or leave amount in the Plan.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity - The Knox County Retirement and Pension Board and System (the “Retirement Board”, “System”) was established by the Tennessee General Assembly, House Bill No. 866, Chapter 246, Private Acts 1967-68, as amended. The powers of the Retirement Board are also governed by the Knox County Charter, Article VII, as amended. The System is considered a part of Knox County, Tennessee and is included as part of the County’s financial reporting entity and is included in the County’s CAFR as pension trust funds, fiduciary fund types.

Basis of Accounting - The System’s financial statements have been prepared using the accrual method of accounting in conformity with U.S. generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB).

Contribution Revenue Recognition - Employee and employer contributions are recognized as additions to the plans net position in the period in which the employee services are performed and respective contributions are due.

Cash and Cash Equivalents - Cash and cash equivalents consist of highly liquid investments, including cash held on a temporary basis by the investment trustee and custodian and money market funds. Substantially all cash and cash equivalents are uninsured and uncollateralized; carrying values approximate fair value.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investment Valuation and Income Recognition - Investments are stated at their estimated fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Net increases (decreases) in fair value of investments reflect the change in market values from the preceding year-end to the current year-end (including investments bought, sold and held during the year). Purchases and sales of securities are recorded on a trade-date basis. Interest and dividend income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

The following is a description of the valuation methodologies used to measure investments at fair value:

Interest-Bearing Deposits and Money Market Funds: Valued at purchase price.

Debt Securities: Values are based upon quotes obtained from national or international exchanges.

Mutual Funds: Valued at quoted market prices which represent the net asset value of shares held by the plans at year end.

Common Collective Investment Trusts: Valued based on the fair value of the collective trust's underlying investments as based on information reported by the investment advisor using the audited financial statements of the collective trust at year-end.

Guaranteed Investment Contracts: The investment contract with an insurance company is not actively traded and significant other observable inputs are not available. Thus, the fair value of the investment contract is determined by analyzing the underlying market value of the insurance company's general underlying investment portfolio.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the plan administrator believes the valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Benefits Paid - Benefit payments to participants are recorded as incurred according to the plan provisions.

Net Plan Position - Net plan position comprises results from investment income (loss), contributions, benefits paid and administrative expenses. Net plan position is classified as follows: restricted for pension and retirement benefits.

Actuarial Present Value of Accumulated Plan Benefits (Defined Benefit Plans) - Accumulated plan benefits are those future periodic payments, including lump-sum distributions that are attributable under the Plan's provisions to the service employees have rendered. Accumulated plan benefits include benefits expected to be paid to (a) retired or terminated employees or their beneficiaries, (b) beneficiaries of employees who have died, and (c) present employees or their beneficiaries. Benefits payable under all circumstances - retirement, death, disability, and termination of employment - are included, to the extent they are deemed attributable to employee service rendered to the valuation date.

The actuarial present value of accumulated plan benefits is determined by an actuary from USI Consulting Group and is that amount which results from applying actuarial assumptions to adjust the accumulated plan benefits to reflect the time value of money (through discounts for interest) and the probability of payment (by means of decrements such as for death, disability, withdrawal or retirement) between the valuation date and the expected date of payment.

Net Position Flow Assumption - The System's net position is restricted for pension and retirement benefits. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. When both restricted and unrestricted resources are available for use, it is the System's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Expenses - Operating expenses of the System, such as salaries, benefits, occupancy costs, and fees charged by the investment custodians, advisors, actuary and third-party administrator are allocated to the defined benefit plans.

Investment fees related to the defined contribution plans participants' accounts are included in net appreciation (depreciation) of fair value of investments.

Use of Estimates - The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the statement of plan net position date, and reported amounts of additions and deductions during the reporting period. Significant estimates include fair value of investments and all actuarial calculations. Accordingly, actual results may differ from those estimates.

Governmental Accounting Standard Board (GASB) Pronouncements

GASB Statement No. 63 - During the year ended December 31, 2012, the System implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting the statement of plan net position and statement of changes in plan net position.

GASB Statement No. 67 - The System plans to adopt GASB Statement No. 67, *Financial Reporting for Pension Plans – an Amendment of GASB Statement No. 25*, required for fiscal periods beginning after June 15, 2013, during calendar year-end 2014. Management is in the process of determining the effects, if any, that the adoption of this Statement will have on the System's financial statements.

GASB Statement No. 68 - The System plans to adopt GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an Amendment of GASB Statement No. 27*, required for fiscal periods beginning after June 15, 2014, during calendar year-end 2015. Management is in the process of determining the effects, if any, that the adoption of this Statement will have on the System's financial statements.

Restatement of Beginning of Year Plan Net Position (Defined Contribution Plans) - The beginning of year plan net position as of January 1, 2012 amounts for the defined contribution plans have been restated to record prior period adjustments related to accounting errors as described in Note 11.

NOTE 3 - DEFINED BENEFIT PLANS - FUNDING POLICY, FUNDING PROGRESS AND FUNDED STATUS

Knox County makes periodic payments to the investment trustee of the defined benefit plans, State Street Bank & Trust, determined on the basis of annual actuarial estimates furnished by USI Consulting Group which shall be in such amounts as the administrator deems necessary for the accumulation to be sufficient to provide applicable retirement benefits. Participants are required to make contributions as described in Note 1.

NOTE 3 - DEFINED BENEFIT PLANS - FUNDING POLICY, FUNDING PROGRESS AND FUNDED STATUS (Continued)

The Plans adopted the use of the individual entry age normal method effective with the January 1, 2009 valuation. As of January 1, 2013, the most recent actuarial valuation date, the defined benefit plans schedule of funding progress and funded status was:

Schedule of Funding Progress	Closed Defined Benefit Plan	Teacher's Plan	UOPP
Actuarial Value of Plan Assets	$ 48,072,000	$ 60,384,664	$ 117,526,735
Actuarial Accrued Liability (AAL)	76,734,548	79,037,520	146,609,127
Unfunded Actuarial Accrued Liability (UAAL)	$ 28,662,548	$ 18,652,856	$ 29,082,392
Funded Ratio	62.65%	76.40%	80.16%
Annual Covered Payroll	$ 2,806,090	$ 117,974	$ 29,784,860
UAAL as a Percentage of Covered Payroll	1021.44%	15810.99%	97.64%
Funded Status			
Annual Pension Costs (APC)	$ 2,416,735	$ 1,151,018	$ 4,620,360
Actual Contributions Made	2,870,544	1,183,029	4,709,512
Percentage Contributed	118.78%	102.78%	101.93%

The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

For the year ended December 31, 2012, the defined benefit plans' actuarial required employer contribution was $8,170,966 which was the normal cost reduced by expected employee contributions plus amortization of the past service base or unfunded accrued liability. During 2012, Knox County made actual employer contributions of $8,763,085. The actuarial value of assets was determined using techniques that smooth the effect of short-term volatility in the market value of equities over a five-year period.

NOTE 4 - DEFINED BENEFIT PLANS – ACTUARIAL ASSUMPTIONS

Significant actuarial assumptions used in the valuation of the defined benefit plans as of January 1, 2013 are as follows:

	Closed Defined Benefit Plan	Teacher's Plan	UOPP
Actuarial Cost Method:	Individual Entry Age Normal Cost	Individual Entry Age Normal Cost	Individual Entry Age Normal Cost
Amortization Method:	Level Dollar Closed Period	Level Dollar Closed Period	Level Dollar Closed Period
Remaining Amortization Period:	19.5 Years	19.5 Years	29.5 Years
Asset Valuation Method:	Greater of the (a) five year moving market average, or (b) 90% of fair value of investments at year-end.	Greater of the (a) five year moving market average, or (b) 90% of fair value of investments at year-end.	Greater of the (a) five year moving market average, or (b) 80% of fair value of investments at year-end.
Actuarial Assumptions:			
Investment Rate of Return Pre and Post-Retirement (Discount Rate)	7.00%	7.00%	7.00%
Projected Salary Increases Pre-Retirement	3.00%	3.00%	3.00%
Assumed Benefit Increases:			
Active Participants	3.00%	3.00%	3.25%
Inactive Participants	2.20%	N/A	N/A
Age at Retirement	65	60	Participants hired before age 40, age 57 and 30 years of credited service. Participants hired after age 40, age 50 and 25 years credited service.
Mortality Table:	1983 Group Annuity (Male and Female)	1983 Group Annuity (Male and Female)	1984 Unisex

NOTE 5 - INVESTMENTS, AT FAIR VALUE

The Knox County Retirement and Pension Board and System's Plan Document and Trust Agreement Section II-A-3, as amended, authorizes the Retirement Board to employ a bank or trust company as the investment trustee and custodian and registered investment advisors. The Trust Agreement permits the Retirement Board to invest in common and preferred stock, mutual funds, bonds and real estate. The Retirement Board has investment policies that limit exposure to investment risks, including credit, interest rate risk, concentration of credit risk, foreign currency and custodial credit risks.

NOTE 5 - INVESTMENTS, AT FAIR VALUE (Continued)

Defined Benefit Plans

Defined benefit plans' investments at December 31, 2012 consisted of:

	Closed Defined Benefit & Teacher's Plans		UOPP		
	Fair Value	Weighted Average Maturities (Years)	Fair Value	Weighted Average Maturities (Years)	Total Defined Benefit Plans
Defined Benefit Plans:					
Debt Investments					
Corporate Bonds	$ 1,335,578	8.8	$ 1,335,018	9.4	$ 2,670,596
U.S. Treasuries	5,473,425	11.0	5,691,906	11.9	11,165,331
Federal Agency Debt Securities	2,079,345	3.5	2,675,795	3.0	4,755,140
Federal Agency Mortgage Backed Securities	4,494,019	3.6	5,487,193	3.8	9,981,212
Total Debt Investments	13,382,367		15,189,912		28,572,279
Other Investment Types					
Mutual Funds	99,899,319	N/A	105,507,211	N/A	205,406,530
Total Defined Benefit Plans	$ 113,281,686		$ 120,697,123		$ 233,978,809

In order to reduce administrative costs, the Retirement Board has elected to combine the investment assets of the Closed Defined Benefit and Teacher's Plans into one trust account at State Street Bank & Trust Company.

Interest Rate Risk - Interest rate risk, in general, is the risk that the value of an investment will decline as interest rates rise. The Board has an approved investment policies for the Defined Benefit Plans which prohibits debt securities with maturities greater than 30 years and is expected to remain interest rate neutral relative to the asset class benchmark. Interest rate risk is disclosed in the preceding table.

Credit Risk - Credit risk is the risk that the issuer, or other counterparty to an investment, will not fulfill its obligations. The Retirement Board’s investment policy requires that the fixed income portfolio maintain an aggregate “A” Standard & Poor’s credit rating. As of December 31, 2012 the Defined Benefit Plan’s debt investment portfolio was in compliance with the Retirement Board’s investment policy as follows:

NOTE 5 - INVESTMENTS, AT FAIR VALUE (Continued)

Defined Benefit Plans (Continued)

Defined Benefit Plans:	Standard and Poor's Credit Ratings								Total as of
	AA+	AA	AA-	A+	A	A-	BBB+	BBB	December 31, 2012
Closed Defined Benefit and Teacher's Plans									
Debt Investments:									
Corporate Bonds	$ 19,779	$ 73,493	$ 82,774	$ 119,104	$ 106,548	$ 660,975	$ 144,329	$ 128,576	$ 1,335,578
U.S. Treasuries	5,473,425	0	0	0	0	0	0	0	5,473,425
Federal Agency Debt Securities	2,079,345	0	0	0	0	0	0	0	2,079,345
Federal Agency Mortgage Backed Securities	4,494,019	0	0	0	0	0	0	0	4,494,019
Total Closed Defined Benefit and Teacher's Plans	12,066,568	73,493	82,774	119,104	106,548	660,975	144,329	128,576	13,382,367
UOPP									
Debt Investments:									
Corporate Bonds	26,372	87,058	71,737	147,734	159,708	585,268	144,957	112,184	1,335,018
U.S. Treasuries	5,691,906	0	0	0	0	0	0	0	5,691,906
Federal Agency Debt Securities	2,675,795	0	0	0	0	0	0	0	2,675,795
Federal Agency Mortgage Backed Securities	5,487,193	0	0	0	0	0	0	0	5,487,193
Total UOPP	13,881,266	87,058	71,737	147,734	159,708	585,268	144,957	112,184	15,189,912
Total Defined Benefit Plans	$ 25,947,834	$ 160,551	$ 154,511	$ 266,838	$ 266,256	$ 1,246,243	$ 289,286	$ 240,760	$ 28,572,279

NOTE 5 - INVESTMENTS, AT FAIR VALUE (Continued)

Defined Benefit Plans (Continued)

Concentration of Credit Risk - The Retirement Board has adopted investment policies that limit the System's exposure to certain classes of investments. The policy requires each asset class to be broadly diversified. As of December 31, 2012 the Defined Benefit Plans' investment holdings, which include debt and mutual fund securities, were in compliance with the Retirement Board's investment policy and were as follows:

Closed Defined Benefit & Teacher's Plans	Fair Value ($ in thousands)	Actual Exposure	Minimum Exposure	Maximum Exposure
Investment Type:				
U.S. Equities	$ 25,823	22%	20%	28%
Non - U.S. Equities	38,636	34%	29%	39%
Core Fixed Income	13,966	12%	10%	14%
High Yield Fixed Income	11,300	10%	8%	12%
U.S. Treasury Inflation Protected Securities	5,706	5%	3%	7%
Private Real Estate	4,603	4%	3%	7%
U.S. Real Estate (REITS)	12,537	11%	8%	12%
Short-Term and Cash and Cash Equivalents	2,742	2%	0%	5%
Total	$ 115,313	100%		

UOPP				
Investment Type:				
U.S. Equities	$ 27,566	23%	20.0%	28.0%
Non - U.S. Equities	42,570	35%	28.0%	39.0%
Core Fixed Income	15,553	13%	11.0%	14.0%
High Yield Fixed Income	12,408	10%	8.0%	12.0%
U.S. Treasury Inflation Protected Securities	5,739	5%	3.0%	7.0%
Private Real Estate	7,769	6%	5.5%	7.0%
U.S. Real Estate (REITS)	9,377	8%	5.5%	12.0%
Short-Term and Cash and Cash Equivalents	1,393	1%	0.0%	5.0%
Total	$ 122,375	100%		

The following individual investments represent 5% or more of each Defined Benefit Plan's net position at December 31, 2012:

Defined Benefit Plans:	Closed Defined Benefit and Teacher's Plans	UOPP
Mutual Funds:		
Schroder Emerging Markets	$ 8,397,394	$ 10,522,168
CG International	14,632,075	0
Adelante Capital Management	12,537,285	9,376,894
Pyramis Selected International	15,606,904	16,215,484
Loomis Sayles High Yield	11,299,812	12,445,841
State Street Global Advisors (SSGA)		
S&P 500 Flagship	20,548,661	22,264,914
Prisa Real Estate	0	7,769,193
SSGA MSCI EAFE Index	0	15,832,551
Total Defined Benefit Plans Mutual Funds	$ 83,022,131	$ 94,427,045

NOTE 5 - INVESTMENTS, AT FAIR VALUE (Continued)

Defined Benefit Plans (Continued)

Foreign Currency Risk - Foreign currency risk is a form of financial risk that arises from the potential change in the exchange of one currency against another. All investments of the Defined Benefit Plans are denominated in U.S. dollars. The non-U.S. equity composite is expected to be fully invested at all times. Cash equivalent exposure will be minimized and limited to 5%. Both developed and emerging market exposure will be used to implement the non-U.S. equity strategy. The investment structure of the non-U.S. equity composite has been developed to mimic the overall profile of the non-U.S. equity market. Approximately 75% to 85% of the non-U.S. equity composite is required to be invested in developed markets while 15% to 20% is expected to be invested in emerging markets.

Custodial Credit Risk - Deposits - The Retirement Board's investment policy requires that investment securities be registered in the name of the System and that investments are held in accounts under trust. In the case of bank deposits (cash and cash equivalents), this is the risk that in the event of a bank failure, the Plan's deposits may not be returned to it. The State Street Global Advisors (SSGA) Short Term Investment Fund (STIF) is used as the default short-term account from which receipts and disbursements flow through the custodian. The fund seeks to provide safety of principal and daily liquidity. The fund is not a money market fund registered with the Securities and Exchange Commission, and is not subject to various rules and limitations that apply to such funds. There can be no assurance that the Fund will maintain a stable net asset value.

Defined Contribution Plans

Defined contribution plans' investments at December 31, 2012 consisted of:

	Asset Accumulation Plan	Voluntary 457 Plan	Medical Expense Retirement Plan	Total Defined Contribution Plans
Defined Contribution Plans:				
Investment Type				
Mutual Funds:				
Bond and Equity Funds	$ 45,901,920	$ 2,557,228	$ 0	$ 48,459,148
Investment Models:				
Fixed	2,367,321	69,551	270,663	2,707,535
Conservative	5,226,967	126,595	2,053,817	7,407,379
Moderate	8,235,118	255,233	1,033,756	9,524,107
Balanced	62,822,675	2,106,608	0	64,929,283
Aggressive	33,954,864	1,369,257	0	35,324,121
Ultra Aggressive	15,929,065	971,729	0	16,900,794
Total Mutual Funds	174,437,930	7,456,201	3,358,236	185,252,367
Guaranteed Investment Contract	24,988,875	716,337	0	25,705,212
Common Collective Trusts	26,556,771	1,086,117	2,100,158	29,743,046
Total Defined Contribution Plans	$ 225,983,576	$ 9,258,655	$ 5,458,394	$ 240,700,625

Concentration of Credit Risk - The Assets Accumulation and Voluntary 457 Plans offer a variety of investment choices to its participants that are measured against various market benchmarks such as the S&P 500, Russell 2000, Barclays 1-5 Year Bond, etc. The Retirement Board monitors the Plans fund's investment performances to determine if the individual fund's results are above the 50th percentile as compared to its peers as measured against the relevant market benchmarks.

The Retirement Board has established for MERP one investment option for plan participant's that consists of 25% fixed, 38% conservative and 37% moderate investment styles.

NOTE 5 - INVESTMENTS, AT FAIR VALUE (Continued)

Defined Contribution Plans (Continued)

Concentration of Credit Risk (Continued)

The following individual investments represent 5% or more of each Defined Contribution Plan's net position at December 31, 2012 :

	Asset Accumulation Plan	Voluntary 457 Plan	Medical Expense Retirement Plan
Defined Contribution Plans:			
Guaranteed Investment Contract:			
TransAmerica Life Insurance Company	$ 24,988,875	$ 716,336	$ 0
Common Collective Trusts:			
Morley Stable Value	18,492,087	836,002	1,087,327
Federated Capital Preservation	0	0	1,012,831
Total Common Collective Trusts	18,492,087	836,002	2,100,158
Mutual Funds:			
Ivy International Core Equity	11,582,540	0	0
Pioneer Cash Reserves	0	0	1,214,689
American Intermediate Bond	0	0	304,677
Calvert Equity Portfolio	0	0	311,404
Total Mutual Funds	11,582,540	0	1,830,770
Total Defined Contribution Plans	$ 55,063,502	$ 1,552,338	$ 3,930,928

Foreign Currency Risk - Foreign currency risk is a form of financial risk that arises from the potential change in the exchange of one currency against another. All investments of the Defined Contribution Plans are denominated in U.S. dollars. The Plans various funds invest in non-U.S. bonds and equities in varying degrees. These funds invest in international developed and emerging markets.

Custodial Credit Risk - Deposits - The Retirement Board's investment policy requires that investment securities be registered in the name of the System and that investments are held in accounts under trust. In the case of bank deposits (cash and cash equivalents), this is the risk that in the event of a bank failure, the Plan's deposits may not be returned to it.

NOTE 6 - TRANSFERS BETWEEN PLANS

During 2012 the System made an operating transfer of $292,884 from the Closed Defined Benefit Plan to the Asset Accumulation Plan of $74,884 for disabled participants who formerly participated in the Closed Defined Benefit Plan and $218,000 for retiree MERP bonuses.

NOTE 7 - RELATED PARTY TRANSACTIONS

Certain defined benefit plans' cash and cash equivalents and investments (mutual funds) are with State Street Bank and Trust Company, or its affiliated entities. State Street Bank and Trust Company is the investment trustee and custodian and, therefore, these investments qualify as related party transactions. The amount of these investments at December 31, 2012 was $62,355,867.

NOTE 8 - PLANS TAX STATUS

The Internal Revenue Service (IRS) has determined and informed the Retirement Board by letters dated April 6, 2011 that the Plans are documented in accordance with the applicable sections of the Internal Revenue Code (IRC). The Plans have been amended since receiving those determination letters. However, the Plan administrator and the Plans' legal counsel believe that the Plans are currently being operated in compliance with the applicable requirements of the IRC. Therefore, no provision for income taxes has been included in the Plans' financial statements. The IRS determination letters expire January 31, 2014 prior to which time the Retirement Board will submit applications for new determination letters.

The Plans are subject to audits by taxing authorities. However, currently no audits for any periods are in progress. The plan administrator believes that the Plans are no longer subject to tax examinations for years prior to December 31, 2009.

NOTE 9 - DEFINED CONTRIBUTION RETIREMENT AND BENEFIT PLANS

The Retirement Board offers to its employee's participation in three different defined contribution retirement plans, that covers certain full-time employees, which includes the Knox County Asset Accumulation Plan, Voluntary 457 Plan and the Medical Expense Retirement Plan. For a description of these Plans see Note 1. During 2012, the Retirement Board's employer matching contributions to these Plans was $35,694 and the employee contributions were $42,005.

NOTE 10 - RISKS AND UNCERTAINTIES

Defined Benefit Plans

Investment securities in general, are subject to various risks, such as interest rate, credit and overall market volatility. Due to the levels of risk associated with certain investment securities, it is possible that changes in the defined benefit plans' values of investment securities could occur and that such changes could materially affect the amounts reported in the Statement Plan Net Position. Employer contributions could be expected to change as well.

Defined benefit plan contributions are made and the actuarial present value of accumulated plan benefits are reported based on certain assumptions pertaining to interest rates, inflation rates and employee demographics, all of which are subject to change. Due to uncertainties inherent in the estimations and assumptions process, it is at least reasonably possible that changes in these estimates and assumptions in the near term could be material to the financial statements.

Defined Contribution Plans

The defined contribution plans provide for various investment options. Investment securities are exposed to various risks, such as interest rate, market and credit risk. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risks in the near term would materially affect participant's account balances and the amounts reported in the Statement of Plan Net Position and the Statement of Changes in Plan Net Position.

Uncertainties

There are no claims or litigation that the System is subject to which management believes would have a significant impact on the Plan's financial statements

NOTE 11 - PRIOR PERIOD ADJUSTMENT

Correction of Accounting Errors - Defined Contribution Plans

During 2012, management, legal counsel and the external auditors re-evaluated the accounting treatment related to the Voluntary 457 Plan financial statements concerning the account balances and transactions of employees who utilized separate investment vendors that were not under a trust arrangement with the Retirement Board. According to U.S. generally accepted accounting principles (GAAP) and the standards prescribed by the Governmental Accounting Standards Board (GASB), activities within a pension trust fund must be accounted for in a trust with assets held by a governmental entity, or pension trust fund, in a trustee capacity for the purposes of paying benefits when they become due in accordance with the provisions of the Plan. The effect of this prior period adjustment was a reduction in total assets and net position of $15,113,526 as of December 31, 2011.

NOTE 11 - PRIOR PERIOD ADJUSTMENT (Continued)

Correction of Accounting Errors - Defined Contribution Plans (Continued)

Before 2012, the System did not record the fair value of unrealized gains (losses) of the defined contribution plans investments in common collective trusts and guaranteed investment contracts. According to GAAP, investments in interest-earning contracts with insurance companies and common collective trusts should be reported at estimated fair value. Previously the System had recorded these investments at contract value. The effect of this prior period adjustment was an increase in total assets and net position of $1,808,870 as of December 31, 2011

As a result, the amount of plan net position, as of January 1, 2012, decreased by $13,304,656 to reflect the cumulative effect of these prior period adjustments.

The following 2011 financial statement line items were affected by the prior period adjustments:

	Asset Accumulation Plan			Voluntary 457 Plan			Medical Expense Retirement Plan			Total Defined Contribution Plans
	As Originally Reported 2011	Effect of Prior Period Adjustments	As Restated 2011	As Originally Reported 2011	Effect of Prior Period Adjustments	As Restated 2011	As Originally Reported 2011	Effect of Prior Period Adjustments	As Restated 2011	As Restated 2011
Statement of Plan Net Position										
Assets										
Cash and Cash Equivalents	$ (108)	$ 0	$ (108)	$ 72	$ 0	$ 72	$ 0	$ 0	$ 0	$ (36)
Investments, at Fair Value	201,617,093	1,711,141	203,328,234	22,335,749	(15,066,316)	7,269,433	5,455,057	50,519	5,505,576	216,103,243
Receivables	36,101	0	36,101	1,374	0	1,374	716	0	716	38,191
Total Assets and Net Position - Restricted for Pension and Retirement Benefits	$ 201,653,086	$ 1,711,141	$ 203,364,227	$ 22,337,195	$ (15,066,316)	$ 7,270,879	$ 5,455,773	$ 50,519	$ 5,506,292	$ 216,141,398
Statement of Changes in Plan Net Position										
Additions										
Investment Income (Loss)	$ (3,202,799)	$ 1,711,141	$ (1,491,658)	$ (43,777)	$ (84,897)	$ (128,674)	$ 47,330	$ 50,519	$ 97,849	$ (1,522,483)
Contributions	16,302,512	0	16,302,512	3,349,916	(1,702,216)	1,647,700	500,188	0	500,188	18,450,400
Total Additions	13,099,713	1,711,141	14,810,854	3,306,139	(1,787,113)	1,519,026	547,518	50,519	598,037	16,927,917
Deductions	17,670,059	0	17,670,059	1,653,393	(1,156,188)	497,205	889,636	0	889,636	19,056,900
Increases (Decreases) in in Net Position - Restricted for Pension and Retirement Benefits	$ (4,570,346)	$ 1,711,141	$ (2,859,205)	$ 1,652,746	$ (2,943,301)	$ 1,021,821	$ (342,118)	$ 50,519	$ (291,599)	$ (2,128,983)

NOTE 12 - SUBSEQUENT EVENTS

Sheriff's Total Asset Accumulation Retirement Plan (STAR) - In November 2012, the Knox County voters approved a referendum to amend the County Charter to close the UOPP defined benefit plan and cease the enrollment for new Sherriff Department Officers (participants) hired after January 1, 2014. During 2013 the Retirement Board is in the process of developing a new defined contribution plan for law enforcement Officers titled Sheriff's Total Asset Accumulation Retirement Plan ("STAR"). Under STAR, if adopted, employees will contribute 6% of compensation with an employer base contribution of 10% and a 2% supplemental employer contribution, with the supplemental contribution to be initially funded through December 31, 2019. Vesting in the base employer contribution will be 100% after completion of 10 years of credited service and the supplemental employer contribution after 15 years. To account for term limits, the elected Knox County Sheriff and Chief Deputy will be 100% vested after eight years of service. The proposed STAR plan is subject to final approval by the Knox County Commission.

Employee Disability Benefit Plan - During 2013, the Retirement Board is developing a new disability plan to cover Knox County and Knox County Board of Education employees who are current participants in the Retirement System. The proposed plan excludes employees or participants who suffer a disability prior to January 1, 2014 and remained covered by either the Closed Defined Benefit or UOPP Plans. Disability benefits are 60% of a participant's pre-disability compensation, offset for Social Security and worker's compensation and adjusted for earnings while disabled. The proposed plan is subject to final approval by the Knox County Commission.

Knox County Development Corporation (KCDC) and the Metropolitan Drug Commission (MDC) - Effective January 1, 2013, KCDC and the MDC transferred their participants' account balances from the System's defined contribution plans to separate plans and trusts.

REQUIRED SUPPLEMENTARY INFORMATION SECTION

KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

SCHEDULE OF EMPLOYER PENSION FUNDING PROGRESS

Last Six Valuation Dates

	Actuarial Valuation Dates	Actuarial Value of Assets (a)	Actuarial Accrued Liability (ALL) (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a)/ c)
Closed Defined Benefit Plan							
	1/1/2013	$ 48,072,000	$ 76,734,548	$ 28,662,548	62.65%	$ 2,806,090	1021.44%
	1/1/2012	53,269,896	75,233,596	21,963,700	70.81%	3,181,621	690.33%
	1/1/2011	60,419,535	75,562,269	15,142,734	79.96%	3,835,987	394.75%
	1/1/2010	61,231,126	75,999,563	14,768,437	80.57%	4,637,314	318.47%
	1/1/2009	56,512,743	75,435,555	18,922,812	74.92%	5,310,881	356.30%
	1/1/2008	79,179,398	79,179,398	0	100.00%	5,112,493	0.00%
Teacher's Plan							
	1/1/2013	$ 60,384,664	$ 79,037,520	$ 18,652,856	76.40%	$ 117,974	15810.99%
	1/1/2012	65,150,937	77,615,350	12,464,413	83.94%	328,419	3795.28%
	1/1/2011	70,428,532	78,267,707	7,839,175	89.98%	823,283	952.18%
	1/1/2010	69,493,440	79,131,091	9,637,651	87.82%	1,050,650	917.30%
	1/1/2009	61,496,011	83,991,358	22,495,347	73.22%	2,018,191	1114.63%
	1/1/2008	83,327,598	84,657,462	1,329,864	98.43%	4,102,017	32.42%
UOPP							
	1/1/2013	$ 117,526,735	$ 146,609,127	$ 29,082,392	80.16%	$ 29,784,860	97.64%
	1/1/2012	112,378,618	146,067,491	33,688,873	76.94%	27,091,364	124.35%
	1/1/2011	108,614,901	136,916,313	28,301,412	79.33%	27,274,742	103.76%
	1/1/2010	103,280,780	128,135,474	24,854,694	80.60%	27,198,799	91.38%
	1/1/2009	85,035,207	115,217,224	30,182,017	73.80%	25,671,228	117.57%
	1/1/2008	97,974,663	104,812,621	6,837,958	93.48%	24,238,059	28.21%

KNOX COUNTY RETIREMENT AND PENSION BOARD AND SYSTEM

PENSION, RETIREMENT AND EMPLOYEE BENEFIT TRUST FUNDS OF KNOX COUNTY, TENNESSEE

SCHEDULE OF EMPLOYER PENSION CONTRIBUTIONS

Last Six Years

	Closed Defined Benefit Plan			Teacher's Plan			UOPP		
Years Ended December 31,	Annual Required Contribution	Actual Contribution	Percentage Contributed	Annual Required Contribution	Actual Contribution	Percentage Contributed	Annual Required Contribution	Actual Contribution	Percentage Contributed
2012	$ 2,378,622	$ 2,870,544	120.68%	$ 1,183,029	$ 1,183,029	100.00%	$ 4,108,886	$ 4,709,512	114.62%
2011	1,497,424	1,335,374	89.18%	1,046,949	1,046,949	100.00%	4,094,421	4,306,371	105.18%
2010	1,218,164	1,218,164	100.00%	1,217,506	1,217,506	100.00%	4,263,867	4,569,658	107.17%
2009	1,877,420	2,127,420	113.32%	1,898,484	1,898,484	100.00%	2,525,395	2,825,187	111.87%
2008	98,387	0	0.00%	198,608	250,000	125.88%	1,910,505	1,910,505	100.00%
2007 (a)	0	100,000	N/A	135,786	135,786	100.00%	N/A	N/A	N/A

Note: (a) The Uniformed Officers Pension Plan (UOPP) was established July 1, 2007.

INTERNAL CONTROL
AND
COMPLIANCE SECTION

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

Members of the Knox County
Retirement and Pension Board
Knoxville, Tennessee

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Knox County Retirement and Pension Board and System (the "System"), a department of Knox County, Tennessee, which comprise the statement of plans net position as of December 31, 2012, and the related statement of changes in plans net position for the year then ended and the related notes to the financial statements, and have issued our report thereon dated August 23, 2013. We qualified our auditor's opinion because we did not perform auditing procedures with respect to the System's defined contribution plans individual participant account balances accumulated from inception, and we were unable to satisfy ourselves as to the basis on which participants' equity is stated as of the beginning and end of year ended December 31, 2012, or the proprietary of the benefits paid to participants during the year then ended. Consequently, we were unable to determine whether any adjustments to these amounts were necessary.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

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

Purpose of this Report

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

Pugh & Company, P.C.

Certified Public Accountants
Knoxville, Tennessee
August 23, 2013