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Title: A MOTION acknowledging receipt of the King County investment pool advisory panel's report on the King County investment pool, accepting its recommendations, and creating an investment pool work group to examine these recommendations and develop options for their implementation.

Sponsors: Bob Ferguson, Larry Phillips

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Attachments: 1. 12796.pdf, 2. 2008-0305 REVISED Staff Report from 06-11-08 OBFMSI.doc, 3. 2008-0305 Staff Report for 05-28-08 OBFMSI.doc, 4. 2008-0305 Staff Report with Attachments for 06-11-08 OBFMSI.pdf

Date	Ver.	Action By	Action	Result
6/16/2008	2	Metropolitan King County Council	Passed as Amended	Pass
6/11/2008	2	Operating Budget, Fiscal Management and Select Issues Committee	Recommended Do Pass Substitute	Pass
5/28/2008	1	Operating Budget, Fiscal Management and Select Issues Committee	Deferred	
5/27/2008	1	Metropolitan King County Council	Introduced and Referred	

Clerk 06/16/2008

A MOTION acknowledging receipt of the King County investment pool advisory panel's report on the King County investment pool, accepting its recommendations, and creating an investment pool work group to examine these recommendations and develop options for their implementation.

WHEREAS, the King County investment pool was established in 1989 to preserve and protect capital and provide a market rate of return on public funds through budgetary and economic cycles and today, holds over four billion dollars in public funds, and

WHEREAS, the investment pool is available to all districts, agencies and public authorities in King

County, except incorporated cities, to invest their cash reserves, and nearly one hundred of these entities have chosen to become participants in the investment pool, and

WHEREAS, between August 2007 and January 2008, four of the investments held by the investment pool became impaired, where impairment is defined by section 210.9 of the King County investment policies as occurring when the investment's credit quality is rated below investment grade, a default has occurred on payment at maturity, or an enforcement event, as defined by the investment's program documents, has occurred, and

WHEREAS, in light of these impairments, the council acting in its oversight role determined a need to conduct a full scale review of the investment pool, including an examination of investment goals, policies, practices, governing structure and relationship with participants, and

WHEREAS, in the past, the council successfully relied on the aid of citizens with expertise in specific fields to conduct reviews of county operations, and

WHEREAS, through Motion 12595, the council created the King County investment pool advisory panel to review the King County investment pool, and

WHEREAS, Motion 12631 appointed three experts from the financial industry to the advisory panel who were selected for their knowledge of financial markets and instruments, public investment pools and macroeconomics, and

WHEREAS, the advisory panel appointees were: John Rose, the former chief executive officer of Seattle Northwest Securities, the region's largest underwriter of bonds; John Dobrowolski, who has thirty years of experience in capital markets, derivatives, risk management, and portfolio management and is the former senior vice president and division executive of market risk for Washington Mutual; and Mary Ellen Mullen who has over twenty-five years of institutional investment experience and is a principal at Bridgebay Consulting LLC, and

WHEREAS, the advisory panel interviewed county staff, reviewed written records, consulted with

outside sources, and relied on its members' professional expertise to produce a report on the investment pool, and

WHEREAS, the investment pool advisory panel has completed its report and submitted it to the council, and

WHEREAS, the report recommends that the county take rapid and forceful action to bring the investment pool in line with industry best practices, and

WHEREAS, the report makes recommendations on how the investment pool can close the gap between its current practices and industry best practices, and

WHEREAS, the council has a long history of responsible stewardship of the public's money, and

WHEREAS, this motion is intended to provide guidance and to create an investment pool work group to advise the executive finance committee as the committee determines the appropriate policies for the management of the investment pool;

NOW, THEREFORE, BE IT MOVED by the Council of King County:

A. **Acknowledgement and thanks.** The metropolitan King County council gratefully acknowledges receipt of the report of the investment pool advisory panel and thanks John Rose, chair, John Dobrowolski and Mary Ellen Mullen for their service to the citizens of King County.

B. **Intent.** It is the intent of the council that the investment pool will be operated in accordance with industry best practices for a governmental investment pool.

C. **Joint legislative and executive branch investment pool work group created - responsibilities - membership.** A King County joint legislative and executive branch investment pool work group is hereby created for the purpose of ensuring that the investment pool meets industry best practices for a governmental investment pool.

1. On or before July 15, 2008, the King County investment pool work group shall submit to council an action plan for bringing the investment pool in line with such industry best practices. Additionally, the

investment pool work group shall be responsible for various reports to the council as prescribed in this motion.

2. The investment pool work group shall be cochaired by the manager of the finance and business operations division and the council policy staff director, or their designees. The work group shall include the managers of the finance and business operations division and the office of management and budget, the council policy staff director, the lead staff to the operating budget, fiscal management and select issues committee, or its successor, the county auditor, the chief accountant and the chief economist, or their designees. The investment pool work group shall be informed by input from pool participants.

D. Outsourced management. To the extent that it is consistent with state and county law, the council accepts the advisory panel's recommendation that the county outsource the management of the investment pool. The council believes the advisory panel's finding that outsourcing is the most cost-effective, efficient and timely way to close the investment pool's current gap with best practices merits further examination.

1. The investment pool work group shall examine the advisory panel's recommendation to outsource the management of the investment pool and develop options to implement this recommendation to the extent deemed appropriate and consistent with state law. If the work group perceives a particular measure to be beneficial to investment pool management but inconsistent with state law, the group shall advise the council of the reasons for its conclusions and the changes necessary to state law to implement such a measure.

2. The investment pool work group shall report its findings to council on or before September 1, 2008. Eleven copies of the report shall be filed with the clerk of the council, for distribution to all councilmembers.

E. Governance. The council accepts the advisory panel's findings that the investment pool's current governing structure does not allow representation from all participants and does not provide policy makers with adequate access to expert advice. The council accepts the advisory panel's recommendation that modifications to the governing structure are needed. The council acknowledges that the advisory panel's recommended modifications may require changes in state or county law.

1. The council recommends the following immediate modifications to the governing structure:

a. The executive finance committee is requested to immediately develop a plan for including advisory representation on the executive finance committee from non-county participants, with the object of implementing this plan as soon as possible, no later than October 1, 2008; and

b. The executive finance committee is urged to request briefings, at least quarterly, with an independent financial advisor who can expertly comment on the county's policies, practices, and portfolio holdings.

2. To address longer term modifications to the governance structure:

a. The investment pool work group shall review the investment pool's governance structure and shall develop options for modifying the governance structure in light of the advisory panel's recommendations that:

(1) the governing structure be modified to eliminate inherent conflicts of interest;

(2) the governing body be supported by a set of external investment professionals;

(3) the governing body avoid categorical restriction of specific types of investment securities and promote diversification; and

(4) the governing body be held directly accountable to all participants; and

b. The work group's review shall include the advisability of implementing the advisory panel's recommendation that the executive finance committee be replaced by an independent board comprised of both county and noncounty participant representatives and three appointed citizen experts.

3. The work group shall present its findings in a report transmitted to the council on or before September 1, 2008, in the form of eleven copies filed with the clerk of the council, for distribution to all councilmembers. The report shall include a discussion of any amendments to Washington state law, King County Code or King County charter that would be required to implement any of the options.

F. Investment goals and metrics. The council accepts the advisory panel's recommendation that the investment pool governing body clearly define investment goals for the investment pool. The council accepts the advisory panel's recommendation that the investment pool immediately implement a set of metrics that

improves transparency regarding risk and expected returns and enables appropriate performance measurement.

1. The investment pool work group shall provide a report on the investment pool's investment goals and metrics.

a.(1) The report shall examine the advisory panel's recommendations regarding:

(a) appropriate investment goals;

(b) the use and selection of one market benchmark and one peer universe benchmark for the entire portfolio, consistent with the investment goals;

(c) the adoption of a comprehensive set of risk and performance metrics to measure, monitor, and manage the investment pool;

(d) the development of a risk limit framework;

(e) the implementation of stress tests; and

(f) the establishment of a contract with a third party to provide reporting for the investment pool.

(2) The report shall examine the panel's recommendation that absent the outsourcing of the management of the investment pool, the appropriate investment goals are those of a constant net asset value fund.

b. The report shall present options for implementing those recommendations it concludes are in the best interests of the investment pool.

2. The investment pool work group should obtain the services of a consultant to provide expert advice to inform this report.

3. On or before September 1, 2008, the investment pool work group shall transmit the report to the executive finance committee, the council and the executive. Eleven copies of the report shall be filed with the clerk of the council, for distribution to all councilmembers.

4. On or before November, 1, 2008, the executive finance committee is urged to implement new investment goals and performance metrics based on the investment pool work group's recommendations as

contained in the report.

G. Infrastructure.

1. The council supports the advisory panel's recommendation that the investment pool's infrastructure be brought in line with industry best practices for a governmental investment pool. The council accepts the advisory panel's specific recommendations in these areas:

- a. technology upgrades to automate reporting and certain aspects of the investment process;
- b. consolidation of assets within one central repository or custodian bank;
- c. establishment of a credit analysis process;
- d. development of improved internal controls;
- e. updated written investment pool policies and procedures;
- f. improved staffing structures to eliminate operational risk;
- g. improved accounting procedures; and
- h. institution of an annual outside audit.

2. The investment pool work group shall review the recommendations of the advisory panel and develop options for enhancing the infrastructure of the investment pool. The options shall include the feasibility of using the services of an external fund manager to the extent permitted under state law. The investment pool work group shall also review the advisory panel's recommendation that additional audits of the investment pool are needed, including audits by an auditor with a specialty in fixed income accounting and periodic internal control audits.

a. These options shall be presented in a report transmitted to the county council on or before September 1, 2008. Eleven copies of the report shall be filed with the clerk of the council, for distribution to all councilmembers.

b. The report shall contain detailed cost estimates for each option and a timeline for implementation.

3. The finance and business operations division is requested to review the advisory panel's

recommendation to consolidate the investment pool's assets with a single custodian bank on or before October 1, 2008.

4. The advisory panel made several recommendations related to the accounting practices of the investment pool. The manager of the finance and business operations division is requested to examine the accounting practices of the pool and present a report to the work group on or before August 1, 2008.

5. On or before November 1, 2008, the executive finance committee is urged to review the King County investment policies in light of the advisory panel's recommendations to ensure the policies reflect current practice and contain policies in the relevant areas. The advisory panel recommended that the updated policies contain a provision requiring an annual review of the investment policies.

H. External relations. The council supports the advisory panel's recommendation that formal channels be created to include participants in the investment pool's policy decision making process. The council supports the advisory panel's recommendation that the investment pool improve communications with participants, the public, and the executive finance committee. The council supports the advisory panel's recommendation that the county review the fee structure of the investment pool. The council supports the advisory panel's recommendation that the investment pool continue to be rated by a nationally recognized statistical rating agency.

1. The manager of the finance and business operations division is requested to inform all participants of the date, time, and place of all executive finance committee meetings and to send a complete agenda for each meeting to all participants five business days before the meeting.

2. As recommended by the advisory panel, the manager of the finance and business operations division is requested to hold an annual meeting beginning in 2008 to discuss the performance of the investment pool during the prior year, solicit participant input on investment pool policies and outline the investment strategy for the coming year. The manager of finance and business operations division is requested to inform all participants of the date, time and place of this annual meeting thirty calendar days before the meeting.

3.a. Beginning on or before August 1, 2008, the finance and business operations division is requested to produce an improved monthly report on the investment pool that includes elements recommended by the advisory panel:

- (1) investments by type and as a percentage of the portfolio;
- (2) a listing of issuers;
- (3) the cost of each investment, its yield to maturity at both cost and market value, accrued interest and maturity date;
- (4) the market value of each investment;
- (5) the par value of each investment;
- (6) total returns for prior periods;
- (7) comparison of current incomes against forecasts and budgeted income projections;
- (8) investments by maturity date;
- (9) average weighted yield to maturity of the portfolio, including comparison to applicable benchmarks;
- (10) percentage of the total portfolio held by each institution; and
- (11) principal and type of investment by fund.

b. The repor should be updated monthly and made available to the executive finance committee, all participants and the public. Eleven copies of the report and each update shall be filed with the clerk of the council, for distribution to all councilmembers.

4. As recommended by the advisory panel, the finance and business operations division is requested to enhance its current website for the investment pool. The website should include general information about the investment pool, a current copy of the investment pool policies, and monthly reports on the investment pool. These enhancements should be operational no later than August 1, 2008, and updated on a monthly basis.

5. The council understands that the executive finance committee is currently undertaking a review of

the investment pool fee structure. The executive finance committee is requested to update the council on its review on or before July 15, 2008.

I. Impaired investments. The council supports the advisory panel's recommendation to bifurcate the impaired investments from the performing investments. The council supports the advisory panel's recommendation that the county obtain the services of a qualified investment manager to advise the county on the management of impaired investments.

1. The executive finance committee is urged to immediately consider the issue of bifurcation.
2. The executive finance committee is requested to immediately obtain the services of a qualified investment manager to advise the county on the management of impaired investments.

J. Audit. The council supports the advisory panel's recommendation that an audit be performed of the treasury operations section of the finance and business operations division to ensure that cash management and investment functions work together efficiently. The council will consult with the county auditor about such an audit.

K. Business review. The council supports the advisory panel's recommendation that the investment pool conduct a business review every three years. The executive finance committee is requested to consider implementing such a review.

L. Quarterly report by manager of finance and business operations division. The manager of the finance and business operations division is requested to report to the council each quarter regarding the specific steps taken and progress made on the recommendations in this motion. The first report shall cover the third quarter of 2008. The manager shall file eleven copies of the reports to the clerk of the council two weeks after the end of each calendar quarter, for distribution to all councilmembers. The last report shall be made in January 2011, unless otherwise determined by motion by the council.