



JAMES L. McINTIRE  
State Treasurer

State of Washington  
Office of the Treasurer  
Local Government Investment Pool

---

October 25, 2016

The Honorable Jay Inslee, Governor  
The Honorable Troy Kelley, State Auditor  
Members of the State Finance Committee  
Members of the Joint Legislative Audit and Review Committee  
Participants in the Local Government Investment Pool

I am pleased to submit this Comprehensive Annual Financial Report (CAFR) of the state of Washington Local Government Investment Pool (LGIP) for the fiscal year ended June 30, 2016. This report has been prepared by the Office of the State Treasurer (OST) pursuant to Revised Code of Washington (RCW) 43.250.080. It includes only activity of the LGIP and does not include data or information related to other state agencies or funds.

Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with OST management. A framework of internal controls has been established by management for this purpose, as well as to ensure information reported in the investment section is reliable. Because the cost of internal control should not exceed anticipated benefits, the objective is to provide reasonable, rather than absolute, assurance that the financial statements are free from any material misstatements.

To the best of our knowledge, the enclosed data are accurate in all material respects and are reported in a manner designed to present fairly the financial position and changes in net position of the LGIP in conformity with generally accepted accounting principles (GAAP). All disclosures necessary to enable the reader to gain an understanding of the LGIP's financial activities have been included. Data presented in the investment section is prepared on a basis consistent with other sections of the report.

The LGIP's financial statements have been audited by Peterson Sullivan LLP, a firm of licensed certified public accountants. The independent auditor concluded the enclosed financial statements are presented fairly in conformity with GAAP. The independent auditors' report is included in the financial section of this report.

Management's Discussion and Analysis (MD&A), immediately following the independent auditors' report, provides a narrative introduction, overview and analysis of the basic financial statements. The MD&A complements this letter and should be read in conjunction with it.

### **LGIP Profile**

The LGIP, created by the Washington State Legislature in 1986, is managed and operated by OST on behalf of participants. The State Finance Committee administers the statute that created the pool and adopts administrative rules and procedures. In 1995, the State Treasurer established the LGIP Advisory Committee to provide advice on the pool's operation. The advisory committee includes 12 members selected from active pool participants. Eight members are appointed by participant associations, and four are appointed by the State Treasurer.

The LGIP operates in a fiduciary capacity as an investment pool within the framework of state laws and regulations. The LGIP serves as an investment vehicle for governmental entities. Eligible entities may invest temporary cash surpluses to take advantage of the volume and management expertise of the state's investment program to earn a competitive rate of return while maintaining security and liquidity.

### **Investment Policies and Practices**

The LGIP is considered extremely low risk. The portfolio is made up of high-quality, highly liquid securities, with relatively short average maturities to reduce the pool's price sensitivity to market interest rate fluctuations and credit risk. The LGIP also has a strong degree of asset diversification to minimize risk and maintain adequate rates of return.

The investment activity is guided by an investment policy, approved by the State Treasurer and follows the standard of the prudent investor. The objectives of the investment practices, in priority order, are safety, liquidity and return on investment. OST invests cash in excess of the daily liquidity requirements of LGIP participants. Investments authorized by statute include: U.S. Treasury and Agency securities, banker's acceptances, repurchase agreements, reverse repurchase agreements, commercial paper, and deposits with qualified public depositories.

The LGIP is managed diligently by professional treasury personnel to protect against losses from market and credit changes. However, the pool is not insured or guaranteed by any government. Therefore, the maintenance of principal is not fully assured.

### **Financial and Economic Information**

The economic condition of the LGIP is based primarily upon investment earnings. Due to the short-term nature of the portfolio, and the types of investments utilized, yields closely follow the targeted federal funds rate. With an average invested balance of \$10.5 billion during the fiscal year, the LGIP produced an average monthly portfolio yield of 0.31 percent. The LGIP exceeded its benchmark by 26 basis points, resulting in \$27 million in additional interest income for participants.

Fiscal year 2016 was marked by sustained monetary policy by the Federal Open Market Committee (FOMC). The FOMC raised its target for the federal funds rate once from July 2015 through June 2016 stating that there had been considerable improvement in labor market conditions, while expecting inflation to rise over the medium term. The targeted federal funds rate began the fiscal year at 0 to 1/4 percent and ended the period at 1/4 to 1/2 percent.

During the period, the FOMC remarked that growth in economic activity expanded at a moderate pace; labor market conditions strengthened, including strong job gains; underutilization of labor resources declined; household spending increased at solid rates; business fixed investment stayed soft; and the recovery in the housing sector improved further. Additionally, inflation continued to run below the FOMC's two percent longer-run objective.

Consistent with its statutory mandate, the FOMC seeks to foster maximum employment and price stability. To support economic recovery and help ensure inflation is at the rate most consistent with its mandate, the FOMC maintained its policy of reinvesting principal payment from its holdings of agency debt and agency mortgage-backed securities, and of rolling over maturing Treasury securities. By keeping holdings of longer-term securities at sizable levels, the FOMC expects to help maintain accommodative financial conditions.

During the first quarter of fiscal year 2017, the FOMC maintained its target for the federal funds rate at 1/4 to 1/2 percent to support continued progress toward maximum employment and price stability. The Committee anticipates that it will raise the target range when it sees further improvement in the labor market and is reasonably confident that inflation will move back to its two percent objective.

### **Major Initiatives**

OST continues to explore the feasibility of offering a longer-term investment fund option to LGIP participants, similar to an intermediate bond fund, to complement the current money market fund option. OST expects to begin operation when market conditions, such as the interest rate environment, are conducive.

### **Awards**

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the LGIP for its CAFR for the fiscal year ended June 30, 2015. This was the nineteenth consecutive year the LGIP achieved this prestigious award. To be awarded a Certificate of Achievement, OST had to publish an easily readable and efficiently organized CAFR that satisfied both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. OST believes this CAFR continues to meet the Certificate of Achievement Program's requirements and will submit it to the GFOA to determine its eligibility for another certificate.

### **Acknowledgments**

The preparation of this report was accomplished with the professionalism and dedicated services of personnel in OST's Accounting Services section and its Investment Division. This CAFR reflects the State Treasurer's commitment to pool participants and citizens of the state of Washington to operate the LGIP in a responsible manner and to maintain financial statements in conformance with the highest standards of financial accountability.

### **Additional Information**

A section of the State Treasurer's website is dedicated to the LGIP, and features information related to performance measures, historical rates, and portfolio holdings. This CAFR, plus additional information for participants and interested parties, may be accessed on the internet at: <http://www.tre.wa.gov/>.

Sincerely,



Shad Pruitt  
Deputy State Treasurer