

MUNICIPAL EMPLOYEES BENEFIT TRUST  
INVESTMENT POLICY STATEMENT

Restated – January 1, 2008  
Amended February 23, 2016

**I. Introduction**

The assets of the Municipal Employees' Benefit Trust (MEBT) will be managed in accordance with this Investment Policy Statement (IPS), unless changes are subsequently approved by the MEBT Trust Committee.

*Purpose of IPS:*

This IPS document provides a framework for the investment management of MEBT. It formally articulates MEBT's Investment Objectives and Guidelines, as well as the responsibilities of the various parties as they pertain to MEBT. This policy statement is designed to:

- provide for prudent selection and monitoring of the MEBT investment vehicles (such as separately managed accounts, mutual funds, commingled trusts, collective funds, stable value funds) interchangeably referred to as Investment Managers;
- allow for sufficient flexibility in the management oversight process to capture investment opportunities as they may occur, while setting forth reasonable parameters to ensure prudence and care in the execution of the investment program;
- ensure that MEBT is managed in the best interest of its participants and beneficiaries;
- achieve MEBT's long term investment goals including producing a real (inflation-adjusted) return of 3.35% while concurrently controlling volatility of MEBT's total portfolio (inflation assumption is 2.50%);
- minimize MEBT's reasonable expenses of investing;
- provide a framework to guide decisions, communicate with Investment Managers, and direct plan administration;
- invest within the limitations established by Federal and Washington State laws and rules.

### Broad Investment Principles

MEBT is managed with a long-term investment horizon, and will approach asset allocation decisions on a strategic, long-term basis. Studies show that adhering to a strategic long-term asset allocation plan in a consistent and disciplined manner will be the major determinant of MEBT's investment performance.

MEBT will be managed on a total return basis. While MEBT recognizes the importance of the preservation of capital, it also acknowledges the theory of Capital Market Pricing – i.e., varying degrees of investment risk should be rewarded with compensating returns. Consequently, MEBT will invest in a well-diversified portfolio.

### Performance Goals

The following investment goals are in keeping with the fiduciary requirements set forth in federal and state law. These are long term goals and consider other factors set out in this IPS.

1. Attempt to provide an annualized real (inflation-adjusted) rate of return of 3.35% over each market cycle which may span up to five to ten years or more (inflation assumption is 2.50%).
2. Diversify in an attempt to control the volatility of the total portfolio of MEBT and to avoid catastrophic loss of principal. MEBT may be comprised of fixed income, equity and convertible securities that may be actively or passively managed. Various techniques, such as short selling, derivatives, futures and leverage may be used periodically within reason.
3. Attempt to meet or exceed the top 45<sup>th</sup> percentile of peers based on a composite return of other similarly managed funds as measured by MEBT's Investment Consultant. This composite ranking will be measured over a moving three and five year review.

4. Attempt to meet or exceed the performance of the composite

**MEBT benchmark:**

<u>Primary</u>	25.20%	Barclay's Capital Aggregate Bond Index
	10.80%	Merrill Lynch High Yield Master II Index
	16.00%	S&P 500 Index
	8.25%	Russell 1000 Growth Index
	8.25%	Russell 1000 Value Index
	4.00%	Russell 2000 Growth Index
	4.00%	Russell 2000 Value Index
	13.50%	MSCI All Country World Index ex-US (ACWI ex-US) Index
	10%	Credit Suisse Liquid Alternative Beta Index

<u>Secondary</u>	25.20%	Barclay's Capital Aggregate Bond Index
	10.80%	Merrill Lynch High Yield Master II Index
	16.00%	S&P 500 Index
	8.25%	Russell 1000 Growth Index
	8.25%	Russell 1000 Value Index
	4.00%	Russell 2000 Growth Index
	4.00%	Russell 2000 Value Index
	13.50%	MSCI All Country World Index ex-US (ACWI ex-US) Index
	10%	Blend of 45% Russell 3000 Index, 15% MSCI All Country World Index ex-US (ACWI ex-US) Index and 40% Barclay's Capital Aggregate Bond Index

This composite ranking will be measured over a moving three and five year review. The MEBT benchmarks for the Investment Managers are indicated in each specific Manager's Investment Manager Guideline (IMG). Benchmarks will be applied retroactively to 12/31/2013.

**II. Asset Allocation**

The following standards are designed to provide a high probability of meeting or exceeding MEBT's return goals, commensurate with the amount of risk in the portfolio. This allocation is based on historical risk/return relationships and is determined after review of the Asset Allocation Study dated May 15, 2013 (attached as Appendix M).

The broad asset allocation for MEBT will be as follows:

Domestic Equities	40.5%
International Equities	13.5%
Fixed Income	36.0%
Liquid Alternatives	10.0%

*Domestic Equity* diversification will roughly be modeled after the Russell 3000 Stock Index as it pertains to market capitalization and style.

*International Equity* diversification will include exposure to various market capitalizations, styles and regions of the world including emerging market securities at the managers' discretion.

*Fixed Income* diversification may include core bond holdings as well as straight high yield debt, foreign debt and convertible securities.

*Liquid Alternatives* are generally considered to be hedging strategies for the overall portfolio. At present, the Liquid Alternative / Global Tactical Asset Allocation strategies approved by MEBT include Investment Company Act of 1940 investment vehicles which are regulated by the Securities and Exchange Commission. They must provide for daily liquidity and daily pricing of the investment vehicle and may use techniques such as short sales, options, derivatives and leverage as approved in their respective prospectus or disclosure document.

	<u>Minimum</u>	<u>Target</u>	<u>Maximum</u>
Domestic Equities	32.4%	40.5%	48.6%
International Equities	10.8%	13.5%	16.2%
Fixed Income	28.8%	36.0%	43.2%
Liquid Alternatives	8.0%	10.0%	12.0%

The targets do not include the Short Term Investment Fund used for liquidity purposes.

### III. General Investment Information

#### Types of Investments

Pooled funds, including mutual funds, exchange traded funds (ETFs), commingled trusts, collective funds, stable value funds as well as separately managed accounts are permissible investment vehicles for MEBT.

#### Types of Securities and Transactions

In general, the following transactions are restricted by MEBT Investment Managers unless specifically addressed in the Investment Manager Guidelines or their Prospectus (or equivalent):

- Short sales
- Selling on margin
- Options
- Derivatives
- Futures
- Forwards
- Swaps
- Leverage

Generally, Separately Managed Accounts will not engage in the types of securities or transactions listed above. However, after careful consideration by MEBT, some investment vehicles may be allowed to engage in using the securities or transactions listed above, provided the prospectus or similar governing document allows such activities.

- Transactions that involve a broker acting as a “principal” where such broker is affiliated with the investment manager or investment consultant are not allowed
- Prohibited transactions between a fiduciary and a party in interest are specifically not authorized

- Investment Managers may purchase the stock of any MEBT party in interest provided such investment would be permitted under ERISA, including its prohibited transaction exemptions; However, Managers using separately managed accounts may not purchase stock of MEBT's designated investment consultant (currently UBS) even if it would be permitted under ERISA, including its prohibited transaction exemptions

*Commission dollars*

Commission dollars are the assets of the Trust, and should generally be used for the exclusive benefit of the Trust.

#### IV. Procedures for Selection and Monitoring Investment Managers

One of the most important tasks of fiduciaries is the selection and monitoring of the Investment Managers or investment funds and subsequent performance. The following outlines the process for such activities.

##### *Criteria for Investment Manager Selection:*

Specific criteria will be established for each Investment Manager search undertaken by MEBT and will be tailored to MEBT's needs.

##### *Required Criteria*

In general, eligible Investment Managers will possess attributes including, but not limited to, the following:

- Be registered with the SEC and demonstrate experience in managing money for institutional clients in the asset class/product category specified by MEBT.
- Display a record of stability in retaining and attracting qualified investment professionals, as well as a record of managing asset growth effectively, both in gaining and retaining clients.
- Demonstrate a sufficient asset base to accommodate MEBT's portfolio. In general, Investment Managers should have at least \$250 million of discretionary institutional assets under management, and MEBT's portfolio should make up no more than 10% of the Investment Manager's total asset base. Exceptions to these criteria may be made under certain circumstances.
- Demonstrate adherence to the investment style sought by MEBT, and adherence to the Investment Manager's investment discipline.
- Fees are competitive with standards for the product category.
- Willing/able to comply with their Investment Manager Guideline.
- Willing/able to comply with certain preferred minimum contracting provisions.

### *Preferred Criteria*

- Outperform the assigned benchmark index in the most recent 3-year and 5-year trailing time periods
- Rank in the top 30<sup>th</sup> percentile of a peer group of similarly managed portfolios in the most recent 3-year and 5-year trailing time periods.
- Provide risk-adjusted returns in the top 30<sup>th</sup> percentile of a peer group of similarly managed portfolios in the most recent 3-year and 5-year trailing time periods.

In addition to the criteria listed above, the Investment Consultant will provide in-depth due diligence on any candidate presented for consideration to MEBT.

### *Criteria for Investment Manager/Fund Monitoring*

The IAC and Investment Consultant will monitor the performance of the Investment Managers each quarter and will clearly note any variations from monitoring criteria listed below.

MEBT reserves the right to terminate an Investment Manager at any time, for any reason. Grounds for terminating an Investment Manager may include, but are not limited to, the following:

- Failure to comply with the IMG's agreed upon for management of MEBT.
- Investing inconsistent with the investment management style.
- Failure to achieve performance objectives specified in the manager's guidelines over a reasonable time period.
- Significant deviation from stated investment philosophy/process.
- Loss of key personnel.
- Evidence of illegal or unethical behavior.
- Lack of willingness to cooperate with reasonable requests by MEBT for information, meetings, or other material related to MEBT.
- Unreasonable or uncompetitive fees.



The presence of any one of these factors will be carefully reviewed by the Investment Consultant and the IAC, but will not necessarily result in an automatic recommendation to terminate.

The IAC may place an Investment Manager on the “watch list” for failure to materially perform any specific goals and objectives set by MEBT. The Investment Consultant will monitor ongoing performance.

Removal from the “watch list” will be considered if and when these goals and objectives have been achieved. The IAC will report any change of status of an Investment Manager to the MEBT Trust Committee on a quarterly basis.

## V. Administration/Operations

### Liquidity

See Appendix (B) for the Liquidity Policy regarding the potential liquidity needs of MEBT. The MEBT Trust Committee will maintain sufficient liquidity in cash equivalent investments to meet expected cash needs. The Cities’ and the participants’ contributions are often sufficient to meet anticipated benefits and will be reviewed periodically.

### Rebalancing Methodology.

Given the volatility of the capital markets, strategic adjustments in various asset classes may be required to rebalance asset allocation back towards the target policy. Such adjustments should be executed so as to minimize excessive turnover and transaction costs. See Appendix (C) for the Rebalancing Policy.

## VI. Responsible Parties, Policies, and Procedures

### Duties of the MEBT Trust Committee

The MEBT Trust Committee approves the investment policies for MEBT. The MEBT Trust Committee will rely on the comments and recommendations of the Investment Consultant and the IAC in making informed, prudent decisions with respect to the following responsibilities. Although the MEBT Committee does not intend to be involved in day-to-day investment decisions, it will be responsible for:

- 1) Establishing financial objectives and setting investment policy, including selecting appropriate asset classes and setting strategic allocations to those asset classes.
- 2) Determining the Investment Manager structure of MEBT.
- 3) Approving the selection/termination of Investment Managers.
- 4) Monitoring investment reports to review objectives.
- 5) Communicating regularly with the Investment Consultant and the IAC. The IAC Chair schedules quarterly IAC meetings, and the MEBT Trust Committee Chair may call an IAC meeting if significant concerns arise about an Investment Manager's strategy, performance, etc.
- 6) Acting to address issues affecting MEBT, (e.g., performance shortfalls, failure of Managers to adhere to guidelines, personnel turnover at Investment Management firms.)

The following actions are the responsibility of the MEBT Trust Committee but will generally involve the advice of the IAC and/or Investment Consultant as appropriate.

- 1) Selection of a qualified master custodian and termination of such custodian when deemed necessary.
- 2) Selection of a qualified investment consultant and termination of such consultant when deemed necessary.
- 3) Setting policies on a system of internal controls to safeguard MEBT Investments.
- 4) As stated below under "Duties of the Investment Managers", proxies are intended to be voted by investment managers who oversee a separately managed account. However, if proxies arise for

investments other than separately managed accounts, they may be cast by the Committee or those parties designated by the Committee, with the best interests of the Plan in mind, and with due consideration given to impacts on Plan participants. The Committee intends to pursue voting of proxies generated by holdings in the Plan only where the value of voting those proxies would have a direct, significant impact on Plan participants. Alternatively, the Committee may seek professional assistance in the voting of proxies generated by holdings in the Plan.

#### *Duties of the Investment Advisory Committee (IAC)*

The MEBT Trust Committee has assigned oversight responsibilities regarding the investment funds of MEBT to the Investment Advisory Committee. The responsibilities of the IAC will be:

- 1) Making recommendations to the MEBT Trust Committee concerning financial objectives and investment policy, including the selection of appropriate asset classes and setting strategic allocations to those asset classes.
- 2) Recommending the Investment Manager structure of MEBT.
- 3) Recommending the selection/termination of qualified Investment Managers.
- 4) Monitoring investment performance at least quarterly against the objectives of MEBT and each Investment Manager. Report to the MEBT Trust Committee on a timely basis.
- 5) Communicating regularly with those responsible for investment results, including periodic reviews with each Investment Manager and an annual report to the MEBT Trust Committee. The IAC Chair schedules quarterly IAC meetings, and may call a special IAC meeting if significant concerns arise about an Investment Manager's strategy, performance, etc. Such communication will be coordinated with and facilitated by the Investment Consultant.
- 6) Recommending actions to address any issues affecting MEBT, e.g. performance shortfalls, failure of managers to adhere to guidelines, personnel turnover at investment management firms retained by MEBT.

### *Duties of the MEBT Investment Consultant*

MEBT utilizes the services of an independent Investment Consultant acting as a fiduciary to provide MEBT/IAC with the following services including, but not limited to:

- 1) Recommending financial objectives and investment policy, including the selection of appropriate asset classes and setting strategic allocations to those asset classes..
- 2) Recommending the Investment Manager structure of MEBT.
- 3) Assisting MEBT in the oversight of existing managers, including monitoring changes in personnel and investment process. Recommending the selection/termination of Investment Managers and negotiating fees. Assisting with negotiation of contract provisions.
- 4) Monitoring investment performance at least quarterly against the objectives of MEBT and each Investment Manager including a review of asset allocation within MEBT. Prepare a quarterly performance report on MEBT's Managers/funds, including a review of asset allocation within MEBT.
- 5) Communicating regularly with those responsible for investment results, including periodic reviews with each Investment Manager. The IAC Chair schedules quarterly IAC meetings, and the Investment Consultant may call a special IAC meeting if significant concerns arise about an Investment Manager's strategy, performance, etc. Coordinate and facilitate communication among the Investment Managers, the IAC and the MEBT Trust Committee.
- 6) Recommending actions to address issues affecting MEBT, (e.g., performance shortfalls, failure of managers to adhere to guidelines, personnel turnover at investment management firms retained by MEBT) or independent research on investment topics.

### *Duties of the Investment Managers*

MEBT will be managed on a discretionary basis by professional external Investment Managers who have been retained for that purpose by MEBT. The Managers will have the following responsibilities. In addition, Managers have specific responsibilities included in their respective Investment Manager Guideline (IMG) Appendix to this IPS.

- 1) Adhere to the investment management style concepts/principles for which they were retained, including, but not limited to: developing portfolio strategy; performing research; developing buy, hold, and sell strategies; purchasing and selling securities;
- 2) Function under a formal contract that delineates its responsibilities and appropriate performance expectations.
- 3) Vote proxies in the best interest of MEBT participants and beneficiaries. Report non-routine issues annually to the IAC.
- 4) Operate in accordance with a specific Investment Manager Guideline (IMG) as acknowledged, in writing and provided as an Appendix to this Investment Policy Statement.
- 5) Have discretion/authority for determining investment strategy, security selection, and timing subject to the IMG.
- 6) Execute all transactions for MEBT on a “best execution” basis.
- 7) Coordinate with Investment Consultant to reconcile accounting, transaction, and asset summary data with custodian valuations and communicate and resolve any significant discrepancies with the custodian and consultant on a quarterly basis.
- 8) Communicate regularly with the Investment Consultant and the IAC on matters such as: major changes in the Investment Manager's investment outlook, investment strategy and portfolio structure; significant changes in ownership, organizational structure, financial condition, or senior personnel; changes in the Portfolio Manager assigned to MEBT; issues which the Manager believes are of significant interest or material importance.

### *Duties of the Master Custodian / Sub-Custodian*

With the possible exception of assets invested in mutual funds or other commingled vehicles, the assets of MEBT will be held in a custody account with a master custody bank or network of sub-custodians with electronic connectivity to the master custodian.

### **VII. Standard of Care**

This policy hereby adopts the investment provisions established in RCW 35.39.060 as the standards for each investment manager. It is as follows: The manager shall act with the care, skill, prudence and diligence under the circumstances then prevailing that a "prudent man" acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims; shall diversify the investments of the employees' pension system so as to minimize the risk of large losses; and shall act in accordance with the documents and instruments governing the employees pension system, insofar as such documents and instruments are consistent with the goals of the IAC / MEBT Trust Committee.

### **VIII. Process for Changing this IPS**

Any changes to this policy statement will be recommended by the Investment Advisory Committee (IAC)/Investment Consultant and subsequently approved by the MEBT Trust Committee. Such changes will be made in writing. These policies will be reviewed annually, or more often as conditions warrant with changes made as appropriate.

The MEBT Trust Committee and the IAC will have discretion to interpret this IPS and apply its judgment, including allowing variances from its specific requirements as it determines are in the best interest of the Trust and its participants.

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Amended August 5, 2009  
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Amended November 26, 2013  
November 18, 2014  
February 23, 2016

Paula Dillon for  
MEBT Secretary Print  
Lucy Liu

Paula Dillon for  
MEBT Secretary Sign  
Lucy Liu  
3/2/16  
Date

Brian W KESSACK  
MEBT Chair Print

BWK  
MEBT Chair Sign  
2/23/16  
Date

Approved as to Form by

Thomson Bennett & McDonald, P.C.  
2/23/16  
Date

- Appendix A - MEBT Asset Styles
- Appendix B - Liquidity Direction
- Appendix C - Rebalancing Policy
- Appendix G - Large Cap Growth - Westfield Capital Management
- Appendix H - Large Cap Value - Eaton Vance
- Appendix J - Small Cap Growth - Baron Capital Management
- Appendix K - International Growth - William Blair
- Appendix M - Asset Allocation Study

Note: Appendices are intentionally not in sequential order. Letters not listed in this document are available for future assignment.



APPENDIX A

**MEBT Asset Styles**

Investments as of February 23, 2016

<b>Asset Style</b>	<b>Target Allocation</b>	<b>Benchmark</b>
Core Bond Plus	25.20%	Barclays Capital Aggregate Bond Index
High Yield Debt	10.80%	Merrill Lynch High Yield Master II Index or Barclays Capital High Yield Index
US Passive Index	16.00%	S&P 500 Index
US Large Cap Growth	8.25%	Russell 1000 Growth Index
US Large Cap Value	8.25%	Russell 1000 Value Index
US Small Cap Growth	4.00%	Russell 2000 Growth Index
US Small Cap Value	4.00%	Russell 2000 Value Index
International Growth	6.75%	MSCI All Country World Index (ACWI) ex US Index and MSCI EAFE Growth Index
International Value	6.75%	MSCI All Country World Index (ACWI) ex US Index and MSCI EAFE Value Index
Liquid Alternatives	3.33%	Credit Suisse Liquid Alternative Beta Index or prospectus benchmark
Liquid Alternatives	3.33%	Credit Suisse Liquid Alternative Beta Index or prospectus benchmark
Liquid Alternatives	3.34%	Bank of America Merrill Lynch USD LIBID 1 Month Average or prospectus benchmark

FRANK W. KESSACK  
MEBT Chair Print

  
MEBT Chair Sign

2/23/16  
Date

