

**POLICY NUMBER:** 2.20.100**EFFECTIVE DATE:** 1/16/14**TITLE:** Labor and Industries' Insurance Funds**SUPERSEDES:** 11/15/12**BOARD ADOPTION:** 1/16/14**APPROVED:** 

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**PURPOSE**

This document outlines the guidelines and investment policy for the Department of Labor and Industries' (L&I) Insurance Funds managed by the Washington State Investment Board (WSIB), and supersedes any prior Board-adopted policies.

**POLICY****Standard of Care**

Under Chapter [43.33A.030](#) RCW, trusteeship of the L&I Insurance Funds is vested in the voting members of the Board. The Legislature has established a standard of care for investment of these funds in Chapter [43.33A.140](#) RCW. Additionally, the Board and its staff must comply with other state laws, such as the Ethics in Public Service Act, Chapter [42.52](#) RCW, as it makes its investment decisions and seeks to meet the investment objectives listed below.

**Strategic Objectives**

In accordance with Chapter [43.33A.110](#) RCW, the portfolio is to be managed to limit fluctuations in the industrial insurance premiums, and, subject to this purpose, achieve a maximum return at a prudent level of risk. Based on this requirement, the order of the objectives shall be:

1. Maintain the solvency of the funds;
2. Maintain premium rate stability;
3. Ensure sufficient assets are available to fund the expected liability payments;  
and
4. Subject to those above, achieve a maximum return at a prudent level of risk.

**Performance Objectives**

The performance objectives are intended to provide the WSIB and L&I with a way to measure the success of this investment policy, the overall asset allocation strategy, and the implementation of that strategy over time. First and foremost the performance of the investment portfolios shall be judged relative to the Strategic Objectives. With the first three criteria met, the actual rates of return of the portfolios will be compared to the Comparable Market Index (CMI) for each fund. The CMI's are developed and calculated by the consultant with the goal to construct a hypothetical passive portfolio with the duration, asset allocation, and appropriate mix of fixed income sectors based on the individual targets for each L&I fund. The return for each fund's portfolio should not be significantly different from that of its CMI over the long term.

**Portfolio Constraints**

- A. All assets under management by the WSIB are to be invested to maximize return at a prudent level of risk in accordance with the requirements of statutes Chapter [43.33A.110](#) and [43.33A.140](#) RCW, which state in part that the WSIB is to "...establish investment policies and procedures designed to attempt to limit fluctuations in industrial insurance premiums, and, subject to this purpose, to maximize return at a prudent level of risk."
- B. No corporate fixed income issue's cost shall exceed three percent of the fund's market value.

**Asset Allocation**

|                           | <b>Target and Ranges</b> |        |
|---------------------------|--------------------------|--------|
|                           | Fixed Income             | Equity |
| Accident Fund             | 90% ±2                   | 10% ±2 |
| Pension Reserve Fund      | 90% ±2                   | 10% ±2 |
| Medical Aid Fund          | 85% ±3                   | 15% ±3 |
| Supplemental Pension Fund | 100%                     | 0%     |

Asset allocation will be reviewed every three to four years, or sooner, if there are significant changes in funding levels or the liability durations.

Market conditions, funding status, and liability assumptions are dynamic, not static; therefore, WSIB staff will meet quarterly with L&I staff to review the investment portfolio.

Assets will be rebalanced across asset classes when market values of the assets fall outside the policy ranges. The timing of any rebalancing will be based on market opportunities, cash flows, and the consideration of transaction costs; therefore, they need not occur immediately.

**Asset Class Structure**

Asset class structure is established by the Board with guidelines for staff to move assets in order to achieve the funds' overall objectives.

**Equity**

The benchmark and structure for U.S. equities will be the broad U.S. stock market as defined by the MSCI U.S. Investable Market Index (MSCI U.S. IMI). The benchmark and structure for non-U.S. equities will be the MSCI All Country World Ex U.S. Investable Market Index (MSCI ACW Ex U.S. IMI). Both portfolios will be 100 percent passively managed in commingled index funds. The commingled funds may use futures for hedging or establishing a long position.

**Equity Allocation**

|                 | Target | Range     |
|-----------------|--------|-----------|
| U.S. Equity     | 60%    | 55% - 65% |
| Non-U.S. Equity | 40%    | 35% - 45% |

### **Fixed Income**

The fixed income portfolios' structure will vary widely among funds depending upon the required duration target.

Accident Fund (608): within plus or minus 20 percent of a duration target of seven.

Pension Reserve Fund (610): within plus or minus 20 percent of a duration target of seven.

Medical Aid Fund (609): within plus or minus 20 percent of a duration target of six.

Supplemental Pension Fund (881): a duration of less than two.

The duration targets will be reviewed every 3 years, or sooner, if there are significant changes in the funding levels or the liability durations.

It is the goal of the fixed income portfolios to match the target durations. Although there may be differences from the targets due to market conditions, over any extended period of time those differences should not be material.

### **Permissible Fixed Income Investments**

Any and all fixed income securities are permissible unless specifically prohibited, including, but not limited to:

1. U.S. Treasuries and Government Agencies;
2. Credit Bonds;
3. Investment Grade Mortgage-Backed Securities as defined by Barclays Capital Global Family of Fixed Income Indices;
4. Investment Grade Asset-Backed Securities as defined by Barclays Capital Global Family of Fixed Income Indices;
5. Investment Grade Commercial Mortgage-Backed Securities as defined by Barclays Capital Global Family of Fixed Income Indices; and
6. Investment Grade Non-U.S. Dollar Bonds.

### **Sector Allocations**

Sector allocations are to be managed within the ranges presented below. These targets are long-term in nature. Deviations may occur in the short-term as a result of interim market conditions. However, if a range is exceeded the portfolios must be rebalanced as soon as it is practical to the target allocations.

#### **Target Allocations for Fixed Income Sectors:**

|   |                  |
|---|------------------|
| U.S. Treasuries and Government Agencies | 5 – 25%          |
| Credit Bonds                            | 20 – 80%         |
| Asset-Backed Securities                 | 0 – 10%          |
| Commercial Mortgage-Backed Securities   | 0 – 10%          |
| Mortgage-Backed Securities              | 0 – 25%          |
| <b>Total Bonds</b>                      | <hr/> 100% <hr/> |

Total market value of below investment grade credit bonds (as defined by Barclays Capital Global Family of Fixed Income Indices) shall not exceed 5 percent of the total market value of the funds.

Although below investment grade mortgage-backed, asset-backed, or commercial mortgage-backed securities may not be purchased, portfolio holdings that are downgraded to those levels or are no longer rated may continue to be held.

The total market value of below investment grade mortgage-backed, asset-backed, and commercial mortgage-backed securities shall not exceed 5 percent of the total market value of the funds.

### **Reporting**

- A. A management information system is to be used for reporting internally to senior staff on the fixed income implementation of this policy. This report is prepared monthly to include, but is not limited to:
  - 1. Current market values and allocations, by sector, compared to the policy ranges;
  - 2. Aggregate and individual portfolio characteristics compared to guidelines; and
  - 3. Delinquencies and defaults.
- B. An executive management report is to be provided to the Board quarterly showing market values and performance.

### **RESPONSIBILITIES**

#### Washington State Investment Board

The Board is responsible for approving the fund's strategic asset allocation and investment policy as well as reviewing the structure, strategy, and performance of the portfolio.

#### Public Markets Committee

The Committee is responsible for recommending the investment policy to the Board.

#### Staff

Staff is responsible for recommending investment policy to the Public Markets Committee, implementing the policy, and reporting to the Public Markets Committee and the Board. Staff is also responsible for recommending strategic asset allocation to the Board.

## **POLICY REVIEW**

The Board shall review this policy at least once every three (3) years to ensure that it remains relevant and appropriate.

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Original Policy Adopted 10/20/92

Revised 6/16/94

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Revised 2/19/98

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