

ADVISORY OPINION

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REFERENCES: RCW 42.52.190

SUMMARY OF CHANGES: No changes.

Permissible Investments/Reinvestment of Dividends

QUESTION

May a state officer or state employee responsible for the investment of public funds satisfy the obligation under RCW 42.52.190(1) to obtain approval for investments that exceed the \$10,000 value threshold at acquisition if the employee makes a one-time disclosure of, and obtains approval for, his or her participation in an automatic reinvestment program?

ANSWER

Yes. RCW 42.52.190(1) allows employees to have a direct or indirect financial interest that exceeds \$10,000 in any property, security, equity, or debt instrument provided the employee receives the written approval of the agency. An agency responsible for the investment of funds may establish a policy that allows for a one-time disclosure of participation in an automatic reinvestment program.

ANALYSIS

This opinion concerns state officers and state employees of the State Investment Board (SIB), an agency responsible for the investment of public funds. The question is whether SIB members and employees comply with RCW 42.52.190(3) if the SIB implements a policy that allows its members and employees to make a one-time disclosure of participation in an automatic reinvestment program. Under an automatic reinvestment program, an investor may direct a company to automatically reinvest any dividends issued in respect of stock already owned to purchase additional shares of that stock. Presumably, the regular reinvestment of dividends will increase the value of the investor's holdings in stock.

By way of illustration, the SIB asks the Board to consider two examples:

Example 1: Individual A, a State Investment Board Member, owns 20 shares of stock in

Corporation X worth \$500 a share, for a total value of \$10,000. The first day of the following month is the beginning of a calendar quarter and Corporation X issues a dividend in the amount of \$10 a share, or \$200 for A. This amount is automatically reinvested to purchase an additional 4 shares of stock for A. Assuming no change in the market value of A's shares, A at the time of acquisition acquired only an additional \$200 worth of stock. The total value of the stock owned by A at the time of acquisition, however, is now \$10,200.

Example 2: Based on the circumstances set out in Example 1, above, A now owns 20.4 shares of stock with a value of \$10,200. At the beginning of the following calendar, quarter, Corporation X uses the dividend to purchase approximately 4 additional stock for A. Again, A acquired only \$204 worth of stock but the stock owned by the investor at the time of acquisition is now valued at \$10,404.

SIB members and employees are subject to RCW 42.52.190, which provides in part that:

(1) Except for permissible investments as defined in this section, no state officer or state employee of any agency responsible for the investment of funds, who acts in a decision-making, advisory, or policy-influencing capacity with respect to investments, may have a direct or indirect interest in any property, security, equity, or debt instrument of a person, without prior written approval of the agency.

...

(3) As used in this section, "permissible investments" means any mutual fund, deposit account, certificate of deposit, or money market fund maintained with a bank, broker, or other financial institution, a security publicly traded in an organized market if the interest in the security at acquisition is ten thousand dollars or less, or an interest in real estate, except if the real estate interest is in or with a party in whom the agency holds an investment.

RCW 42.52.190(2) requires agencies responsible for the investment of funds to adopt policies governing the approval of investments that exceed the permissible \$10,000 threshold under subsection (3). Pursuant to this requirement, the State Investment Board has adopted a rule governing conflicts of interest under WAC 287-04. Under this rule, the SIB's purpose statement declares that:

The board finds that the trusteeship and investment management of the state's trust and retirement funds demand the highest degree of confidence from the beneficiaries of the funds and the public in general, and the establishment of rules regarding conflict of interest and ethical conduct will promote and sustain public trust and maintain integrity in government. WAC 287-04-020.

Under WAC 287-04-032, the SIB requires its employees, executive director, and board members to obtain prior written approval if they, or an immediate family member, purchase any

investment, other than a permissible investment. Under this administrative rule, in the examples provided above, the investor would have to request SIB approval each time an investment exceeds the \$10,000 threshold. The Board assumes that SIB board members or employees seeking to invest in other than permissible investments also may have a request for approval denied if there is reason to believe that the investment may create the potential for a conflict of interest in the performance of public duties.

The Board recognizes that it has become increasingly common for investors to opt for the automatic reinvestment of dividends as a cost effective means of increasing share holdings, and that this type of investment strategy likely was not anticipated by the requirements under RCW 42.52.190(3). The Board believes that the purpose of RCW 42.52.190 is to allow for the disclosure of and approval for investments other than those permitted under subsection (3), and to give the investing agency the ability to address potential conflict of interest concerns through the development of its own policies. This purpose is not altered if the SIB adopts a policy allowing for the one-time disclosure of participation in an automatic reinvestment plan, even though at each successive acquisition under the plan the total value of the shares of that stock may exceed \$10,000 in value. The Board expects that the SIB will continue to monitor the investments of its board members and employees, recognizing that disclosure, particularly in matters relating to the investment of funds and personal financial holdings, is not always sufficient to remedy a conflict of interest.