

INTRODUCTORY
SECTION



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June 2, 2010

Honorable County Executive,
Members of the County Council,
and *Pierce County* Residents:

TRANSMITTAL LETTER

I. INTRODUCTION

I am pleased to transmit to you the 2009 Comprehensive Annual Financial Report of *Pierce County*, Washington. This report was prepared by the Budget and Finance Department to present the financial position of the county at December 31, 2009, and the results of its operations and the cash flows of its proprietary funds for the year then ended. Responsibility for accuracy of the data presented, and completeness and fairness of presentation, including disclosures, rests with the county.

The report is prepared using the governmental financial reporting model required by Generally Accepted Accounting Principles. This reporting model provides a clear fiscal picture of the county as a single unified entity while continuing to provide traditional fund-based financial statements. Each perspective, government-wide and major fund reporting, allows the reader to address relevant questions; provides a basis for comparison (year-to-year, or government-to-government); and enhances county accountability.

The Office of the State Auditor conducts annual financial and compliance audits as required by state statutes. The 2009 audit of county financial statements was conducted in accordance with generally accepted auditing standards and resulted in an unqualified audit opinion.

The independent audit of the financial statements was part of a broader, federally mandated "Single Audit" designed to meet special needs of federal grantor agencies. Standards governing Single Audit engagements require the independent auditor to report not only on fair presentation of the financial statements, but also on the audited government's system of internal controls and compliance with legal requirements. Special emphasis is placed on internal controls and legal requirements involving the administration of federal awards. Reports on internal control and compliance with legal requirements are available in the separately issued Single Audit Report.

The county also maintains an internal audit function to insure adequacy of internal accounting controls. The accounting system is structured to facilitate the effectiveness of such internal accounting controls. Internal accounting controls are designed to provide reasonable assurance that assets are safeguarded and that financial records are reliable for preparing financial statements and maintaining accountability of assets. In addition, the Performance Audit Division of the County Council conducts operational audits of county agencies.

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



II. PROFILE OF THE COUNTY

Pierce County was incorporated in 1852 and operates under a Home Rule Charter adopted by voters in November 1980. The county is organized under the executive-council form of government. Elected administrative officials include the County Executive (the chief executive officer), Prosecuting Attorney, Assessor-Treasurer, and Auditor. The seven-member County Council is elected by district and constitutes the policy-setting legislative body of the county. All elected officials serve four year terms.

This report includes all funds, departments, and entities for which the county is considered financially accountable. While most funds in this report pertain to the entity "*Pierce County Government*", certain *Agency Funds* represent county custodianship of assets belonging to independent governments and special districts. The County Executive is the *ex officio* treasurer for all special purpose districts in *Pierce County*, excluding cities and towns. The Director of Budget and Finance is responsible for duties of the comptroller and treasurer. Monies received from or on behalf of special purpose districts are deposited in a central bank account. The Director of Budget and Finance disburses or invests the monies according to instructions from the respective special purpose district governing body or administrative officer. There are no related organizations which warrant inclusion in the reporting entity.

OVERVIEW

Pierce County is located on scenic Puget Sound and covers 1,794 square miles (1,676 square miles of land and 118 square miles of water). The county boasts ten hospitals, fifteen public school districts, a large number of private schools, two vocational technical colleges, two community colleges, and six 4 year colleges or universities.

The county provides certain services on a countywide basis and other services only to unincorporated areas of the county. Within the appropriate jurisdictions, the county provides law enforcement, criminal detention, fire prevention, judicial administration, parks and recreation facilities, planning and zoning, road maintenance and construction, a sewage disposal system, human services, tax assessments and collections, community development, and general administrative functions.

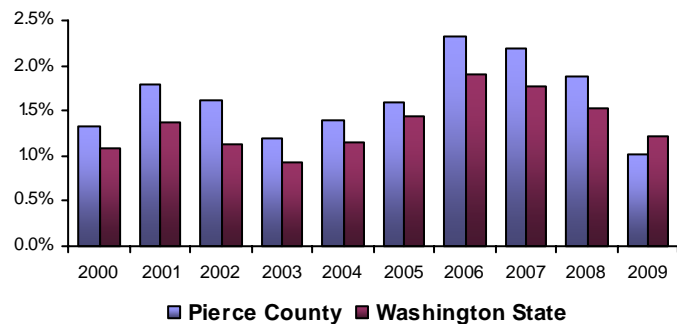


DEMOGRAPHICS

Pierce County is home to an estimated 813,600 people, the second largest county in Washington. County population increased 17.6% from 691,500 in 1999 at an annual average growth rate of 1.6%.

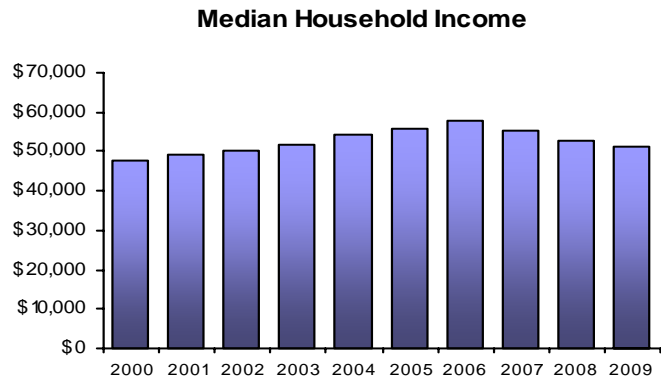
Approximately 53% of *Pierce County* residents live in cities and towns. The five largest cities are Tacoma (203,400), Lakewood (58,840), Puyallup (38,690), University Place (31,500), and Bonney Lake (16,500).

Percentage Change in Population



Source: Office of Financial Management

Median household income for residents of *Pierce County* increased approximately 8% from 2000 to 2009. During this period, the Seattle/Tacoma inflation rate was 28%. However, median household income has declined in 2007, 2008, and 2009 reflecting the effects of the recent economic conditions.



Source: Office of Financial Management

BUDGET POLICIES

In accordance with the *Pierce County* Charter, the County Council is required to adopt annual budgets for all budgeted funds. Income is periodically estimated, and if projections are less than anticipated, the council may reduce appropriations as necessary to keep expenditures within income. The council may also modify the budget on an emergency basis by appropriating contingency funds, revenues received in excess of budgeted revenues, or funds from any other legally available source.



The legal level of budgetary control, the level at which expenditures may not legally exceed appropriations, is the fund level for all funds except for the *General Fund*, which is budgeted at the department level. The county charter also requires proprietary fund budgets though these are not presented in this report.

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III. ECONOMIC CONDITIONS

“The *Pierce County* economy withstood some of the negative effects from the national recession for much of 2008. But growth did slow. *Pierce County’s* slower growth was significantly better than the national experience principally due to *Pierce County’s* military and health care sectors. The slowing *Pierce County* economy in late 2008 indicated more problems on the horizon. The *Pierce County* slowdown became a recession in 2009. Economic activity in *Pierce County* will continue downward, but more moderately as this year [2009] comes to a close. The recession in *Pierce County* will continue through the first half of 2010. It will come to an end during the third quarter of the year. The current recession then, will be the deepest, longest and most severe in the past forty years. A recovering U.S. economy combined with expansionary fiscal and monetary programs will help the local economy. Most of *Pierce County’s* trading partners will be growing again, helping the trade sector. But a stronger dollar will offset some of those gains. Single-family housing activity will improve during the year, as mortgage markets recover and credit becomes available. However, commercial and industrial real estate activity will be depressed for most of 2010. The local health care and military sectors will continue to fuel economic activity, but at a slower rate. The benefits of the national recovery, increased trade flows, some new military construction spending and a recovering housing market will be enough to offset the negative effects of Russell Investments moving out of the area.”

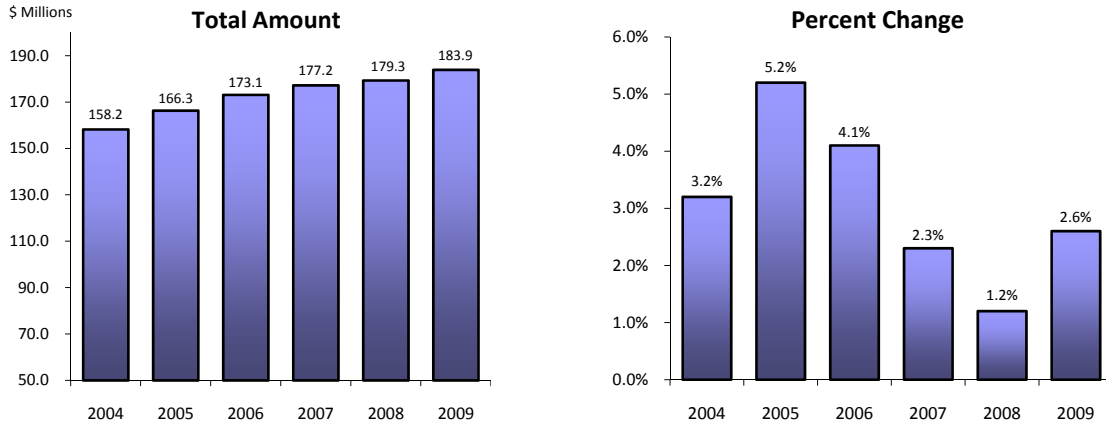
(Quote from Tacoma-Pierce County Chamber, *Pierce County Economic Index Report*, 2010)

The following indicators are key elements for evaluating current economic conditions and are useful when developing projections or economic forecasts.

PROPERTY AND OTHER TAXES

Property taxes and other related taxes are a major revenue source for *Pierce County*. Beginning in 2002, property tax revenue was impacted by the I-747 limit of a 1% increase from existing property. Revenue growth in excess of 1% is due to property taxes from new construction.

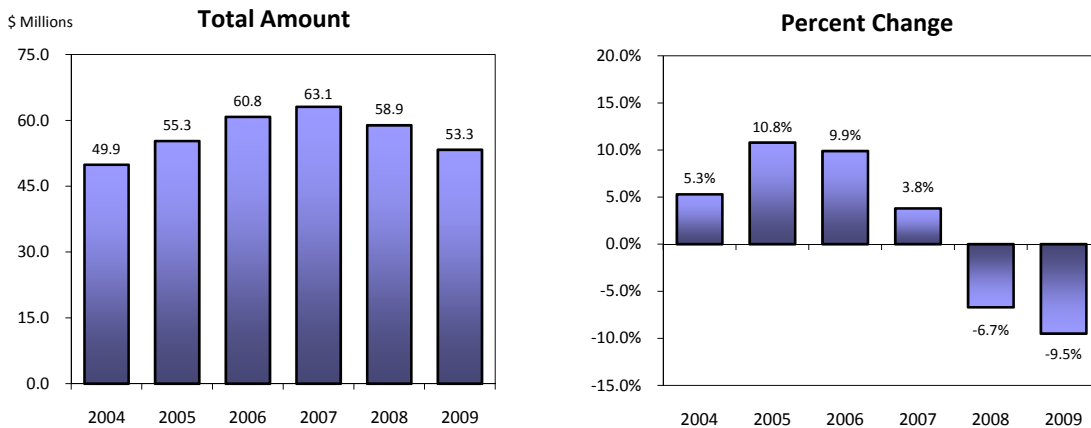
**Property and Other Taxes, 2004–2009
(Total Revenues)**



SALES AND USE TAXES

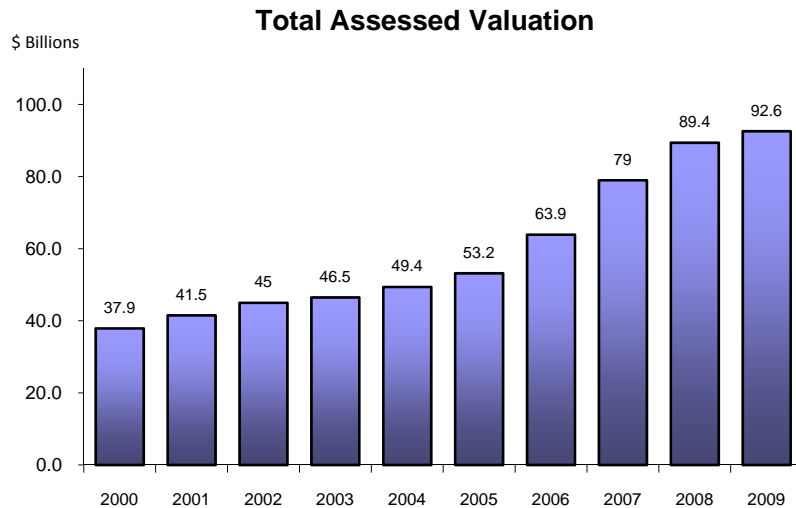
Revenues from sales and use taxes typically provide a stable source of funding. Growth occurs in “normal” years simply because of inflation, population increase, and fluctuations in the strength of the local economy. Total sales and use taxes increased annually until the economic downturn in 2008 and 2009. The trend of decrease is expected to continue into 2010.

**Sales and Use Taxes, 2004–2009
(Total Revenues)**



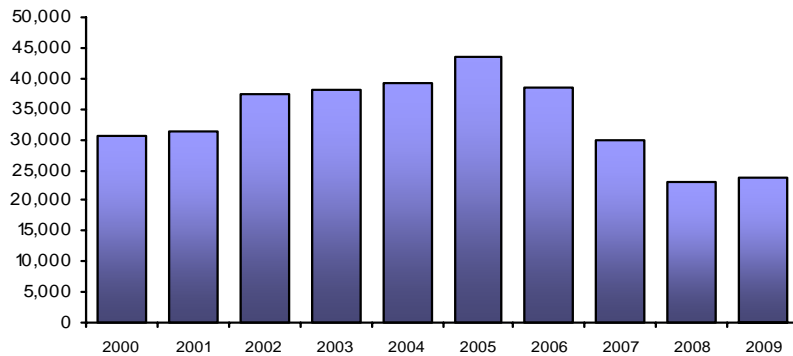
HOUSING AND REAL ESTATE

Assessed value provides a relatively stable base for property tax revenues. Like the rest of the state and nation, *Pierce County*, experienced a “hot” housing market until recently. Between 2005 and 2007 assessed values increased at double-digit rates. Assessed value continues to increase, though, the growth rate in 2009 declined to 3.6%.



Real estate activity is an important economic indicator that greatly impacts property tax revenues and affects operations and workload in areas such as planning, permits, land services, public works, and public construction. After significant declines in 2006 thru 2008, the number of excise tax affidavits processed in 2009 increased 3%.

Excise Tax Affidavits Processed

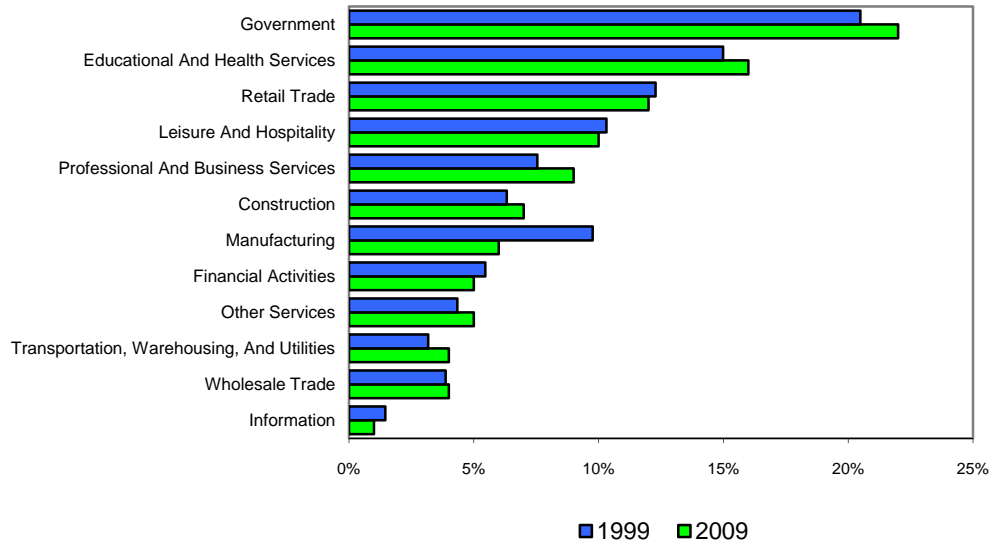


Source: Pierce County Auditor

EMPLOYMENT

Historically the economy of *Pierce County* has been manufacturing and resource based. However, current local, regional, state, and national trends all indicate a shift from manufacturing to government, educational and health services, professional and business services, and construction. The shift in nonagricultural employment is evident in the comparative graph of 1999 and 2009 presented on the following page.

Percentage Employment by NAICS Category



Based on estimates from the *Economic Development Board*, the top twenty major nongovernment employers in *Pierce County* for 2009 include:

| Rank | Organization | Employees | Industry |
|------|--|-----------|---------------------------------|
| 1 | MULTICARE HEALTH SYSTEM | 6,204 | Health Services |
| 2 | FRANCISCAN HEALTH SYSTEM | 4,406 | Health Services |
| 3 | FRED MEYER STORES * | 2,321 | Retail |
| 4 | EMERALD QUEEN CASINO** | 1,915 | Casino Gaming |
| 5 | WAL-MART * | 1,820 | Retail |
| 6 | BOEING COMPANY, THE (Frederickson Site) | 1,537 | Aerospace |
| 7 | SAFEWAY STORES, INC. | 1,261 | Retail (Grocery) |
| 8 | COSTCO | 1,134 | Wholesale |
| 9 | STATE FARM INSURANCE COMPANIES | 1,124 | Insurance |
| 10 | RUSSELL INVESTMENTS | 1,042 | Investment Management |
| 11 | INTEL CORPORATION | 1,000 | Computer Electronics |
| 12 | LONGSHORE LABOR UNION | 976 | Labor Union |
| 13 | MCDONALD'S RESTAURANTS** (Corporate stores only) | 939 | Fast Food |
| 14 | COMCAST CABLE | 934 | Cable Services |
| 15 | ALBERTSON'S INC** | 886 | Retail (Grocery) |
| 16 | DAVITA | 844 | Health Services |
| 17 | MILGARD MANUFACTURING, INC. | 796 | Glass & Window Mfg. |
| 18 | PACIFIC LUTHERAN UNIVERSITY | 707 | Education |
| 19 | AAFES (ARMY & AIR FORCE EXCHANGE SERVICE) | 700 | Merchandise for Armed Forces |
| 20 | KEYBANK | 700 | Banking |

* FTE count was not available for some employers. Headcount was used for these companies.

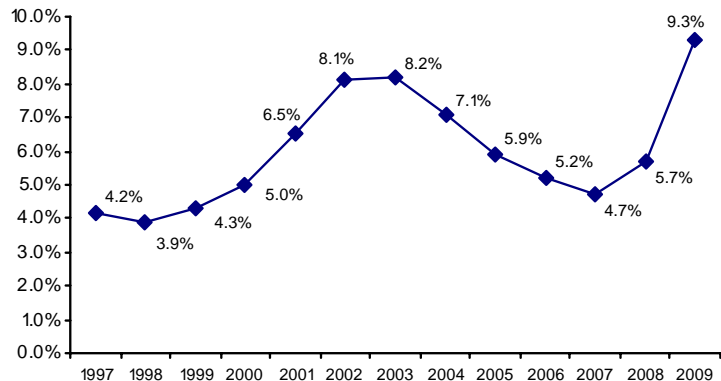
** 2008 numbers were used for employers that did not report current FTE totals in 2009.

The largest employers in *Pierce County* are federal and state government agencies. The federal government employs over 58,000 residents of *Pierce County*. Joint Base Lewis-McChord occupies 91,000 acres in southwest *Pierce County* and employs over 50,000 military and civilian personnel. In addition, local governments and agencies employ over 35,000 county residents: the State of Washington employs over 8,000 people; *Pierce County* employs over 3,000 people; and another 3,000 people are employed at community colleges, technical colleges, and the University of Washington at Tacoma.

Unemployment. For 2009, the average annual unemployment rate for the Tacoma/Pierce County area was 9.3%, which is 0.3% higher than the rate of 9.0% for the State of Washington.

The local unemployment rate had experienced a steady decline prior to the downturn in the economy, decreasing from 8.2% in 2003 to 4.7% in 2007.

Tacoma-Pierce County Average Annual Unemployment Rate



Source: Washington Employment Security

Port Facilities. A major gateway to Asia and Alaska, the Port of Tacoma is a leading North American seaport, the seventh largest container port in North America. Located on Commencement Bay, a natural, deep-water harbor in south Puget Sound, the port has 2,400 acres used primarily for shipping terminal activity, warehousing, distributing, and manufacturing. The Port of Tacoma is an independent municipal corporation created by *Pierce County* citizens in 1918 and authorized to operate under state-enabling legislation.



Reflecting the global recession and its effects on U.S. consumer demand and shipping, the Port of Tacoma's container volumes during 2009 were down 17 percent, with the Port handling 1.5 million TEU's. Additional indicators of Port activity during 2009 follow.

2009 Trade Highlights:

Total TEUs: 1.5 million
Intermodal lifts: 283,820
Total tonnage: 17.4 million short tons
Auto units: 117,357
Grain: 6.5 million short tons

Breakbulk cargo: 92,501 short tons
Vessel calls: 1,221
Value of foreign trade: \$25.27 billion
Value of domestic trade: \$3.5 billion

FUTURE CONCERNS AND DEVELOPMENTS – LONG RANGE PLANNING

Although net asset balances for most county funds remain positive, Pierce County faces several challenges that will require earnest attention during the next few years. These issues affect the county long range planning forecasts and add a significant element of uncertainty to those forecasts as follows:

- ✦ **Public Safety.** Workload levels in law enforcement and the judicial system are expected to continue increasing in the near future.
- ✦ **Jail Operations.** The new adult corrections facility opened in 2005. Related annual jail expenses, including both debt service and operations, continue to increase significantly each year. We anticipate additional fiscal pressure in future years as the inmate population continues to grow.
- ✦ **Economic Growth Slowing.** The strong growth trend in the local economy witnessed in the county over the last several years has reversed itself with the recent recession. This economic slowdown is expected to have a negative effect on *General Fund* revenues in 2010 and possibly thereafter.
- ✦ **Property Tax Payments.** Projected property tax revenues are based on trends over the last ten years. However, the increasing number of homeowners who are delinquent in their mortgage payments or who are actually in foreclosure is a major concern that could adversely affect property tax revenues in the short term.
- ✦ **Federal and State Grants.** Budget cutbacks at either the state or federal level could result in reductions in grants that currently provide substantial support for several major county programs.
- ✦ **Transportation.** Growth in the local economy and population increases are placing substantial pressure on transportation infrastructure. Several funding options are being considered to expand transportation infrastructure capacity and relieve congestion.

Pierce County participates in certain long-range planning processes working locally and regionally to develop and implement economic strategies with the goal of ensuring long-term economic prosperity in the central Puget Sound region, including the following:

- ✦ **Prosperity Partnership.** In 2004, the Puget Sound Regional Council (PSRC) created the Prosperity Partnership; a coalition of business, government, academic, labor, and nonprofit organizations from King, Kitsap, Pierce and Snohomish counties dedicated to developing and implementing an economic strategy to ensure long-term regional prosperity. In September 2005 the coalition adopted the Regional Economic Strategy to both meet the needs of industry clusters, and to strengthen general underpinnings of the regional economy.
- ✦ **Economic Development Goals.** Beginning in 2003, *Pierce County* commissioned a series of studies which evaluated effective ways to help the local economy as an engine of job creation, evaluated how the local economy fits into the regional economy, and defined six goals with action strategies for economic development. An interdepartmental county team developed a work plan and timetable for full implementation of the following six goals:

- Enhance Economic Development Department's Role and Responsibilities
- Proactive Infrastructure Planning
- Strategic Industrial Land Capacity Planning
- Implement Business Climate Improvements
- Enhance Infrastructure Investments
- Enhance Communications to County Departments, Businesses and Jurisdictions

FINANCIAL POLICIES

The county maintains a set of financial policies to guide fiscal and budgetary decision making including:

- ✦ **County Investment Policies and Procedures** provide guidance for investment management.
- ✦ **County Debt Management Policies** outline goals and procedures for financing county operations.
- ✦ **Budget and Finance Department Fiscal Policies** provide guidance in the following areas:
 - Budget Preparation and Monitoring
 - Revenue Sources and Uses
 - Fund Balance Management
 - Expenditure Authorization and Control

MAJOR INITIATIVES

Although several initiatives involving changes to programs and services commenced or were in progress in 2009, most will not have a major impact upon the future fiscal position of *Pierce County*. However, a few such initiatives were of major significance in 2009 as follows:

- ✦ **Mental Health Transition.** The county ended the mental health services contract arrangement with the State and its vendor, and closed the mental health facility in October 2009. Fund balance will likely be sufficient to fund closure costs. Any remaining fiscal issues will be addressed in 2010.
- ✦ **Adult Detention.** Major remodeling of the main jail housed in the County-City Building was substantially completed, including general jail facility improvements and other repair projects.
- ✦ **Parks and Recreation Facilities.** Two major projects, Ashford Park and Cushman Trail were substantially completed. Other parks construction and improvement projects are also currently underway. These projects will be funded by parks related sales taxes and real estate excise taxes. Future operating costs will also be financed by parks sales taxes and additional cooperative funding arrangements with various cities within the county.
- ✦ **River Improvement.** Major floodplain real estate was acquired, funded in part by grants, for flood control purposes.

CASH MANAGEMENT

At year-end, *Pierce County* managed invested funds with a fair market value of approximately \$990 million (excluding investments held by trustees). Funds invested for the direct benefit of *Pierce County* were valued at \$384 million at year-end. The balance of approximately \$606 million was invested for the direct benefit of other taxing districts for which the county serves as treasurer. At December 31, 2009 the investment portfolio of county operating and trust funds (excluding other taxing districts) included types of investment and related maturities as follows:

| <u>Type of Investment</u> | <u>Amount (In Thousands)</u> | <u>Percent of Portfolio</u> |
|---------------------------|----------------------------------|-----------------------------|
| State Investment Pool | \$ 245,068 | 63.78 % |
| Certificates of Deposit | 98,000 | 25.51 % |
| U.S. Government Agencies | 41,149 | 10.71 % |
| Total | <u>\$ 384,217</u> | <u>100.00 %</u> |

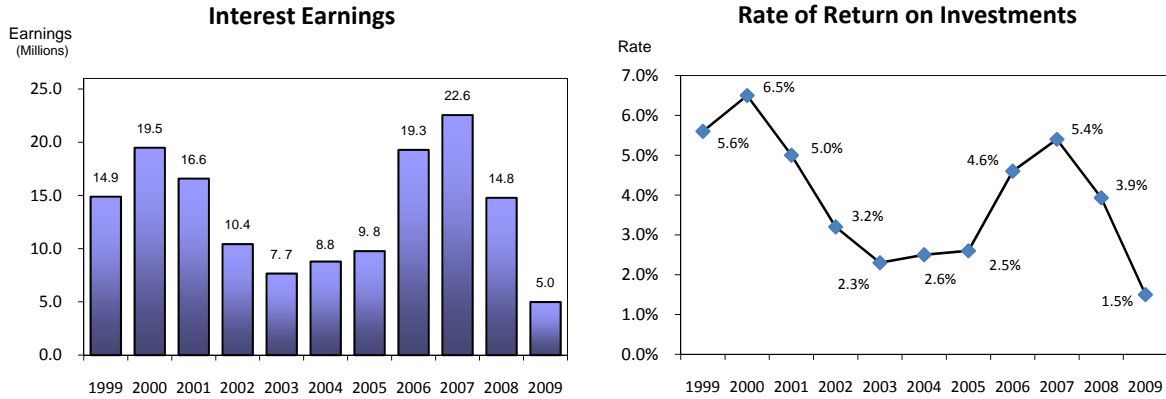
| <u>Days to Maturity</u> | <u>Amount (In Thousands)</u> | <u>Percent of Portfolio</u> |
|-------------------------|----------------------------------|-----------------------------|
| 1-30 | \$ 141,980 | 36.95 % |
| 31-90 | 181,088 | 47.13 % |
| 91-180 | - | 0.00 % |
| 181-365 | 20,000 | 5.21 % |
| Over 1Year | 41,149 | 10.71 % |
| Total | <u>\$ 384,217</u> | <u>100.00 %</u> |

The average yield on county invested funds for 2009 was approximately 1.46%. Total interest earnings on county funds were \$4.99 million, representing a decrease of \$9.79 million from 2008. Both the yield and total interest earnings include the negative impact of \$304 thousand in decreases of fair market value during 2009. The net decreased interest earnings resulted from a decrease in average yield on investments (as adjusted for the fair market value gains) and from a decrease of approximately \$35.2 million in the average daily balance of invested funds.

As is evident from the following graphs, interest earnings declined dramatically in 2000 through 2003 due to the sharp drop in short term interest rates. This trend reversed in 2006 and generated significant interest earnings gains in both 2006 and 2007. In 2008 and 2009 both interest rates and interest earnings again fell due to the actions of the Federal Reserve Board to maintain low interest rates.

Comparative figures for interest earnings and rates of return for county funds invested during the past ten years are presented in the figures shown below:

Interest Earnings and Rates of Return



Investment income includes adjustments to reflect the fair market value of investments. These adjustments (both positive and negative) in fair market value during the current year, however, do not necessarily represent trends that will continue; nor do they indicate that such gains or losses will be realized, especially in the case of investments that the government intends to hold to maturity.

RISK MANAGEMENT

Pierce County maintains an active risk management program emphasizing loss prevention, safety, and coordination of related third party insurance purchases.

The *Self-Insurance Fund* is responsible for managing legal claims for damages asserted, paying any claim settlements, assessing interfund charges to county funds and purchasing related risk insurance policies. Interfund charges are based primarily on the loss experience of the various contributing funds.

The *Workers Compensation Fund* manages and accounts for the workers compensation self-insurance program. The risk management department works with an experienced service company to administer the program. Funding is provided through interfund premium charges to county departments.

The county has established two risk management goals. The first is to maintain a minimum cash and investment balance of at least \$20 million in the *Self-Insurance Fund* and \$1.0 million in the *Workers Compensation Fund*. Such balances are deemed sufficient to fund two very large losses in each program. A second goal is simply to achieve positive net assets for each fund.

| (In Thousands) | Self-Insurance | | Workers Compensation | |
|-----------------------------|----------------|-----------|----------------------|----------|
| | 2001 | 2009 | 2001 | 2009 |
| Cash and Investment Balance | \$ 13,624 | \$ 27,121 | \$ 1,312 | \$ 36 |
| Unrestricted Net Assets | \$ 4,692 | \$ 16,155 | \$ (270) | \$ (827) |

As indicated in the comparison above, the cash/investment balance and related net assets have increased significantly for the *Self-Insurance Fund* from 2001 thru 2009, and continue to meet the above stated goals. However, cash and investment balances, and net assets of the *Workers Compensation Fund* have remained below the goals due to recent negative trends experienced in claims expenses. The *Workers Compensation Fund* continues to actively manage loss prevention and safety programs; and will implement rate increases to eliminate the deficit in net assets.

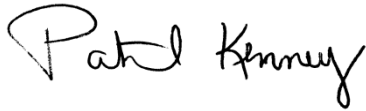
IV. AWARDS AND ACKNOWLEDGEMENTS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to *Pierce County* for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended December 31, 2008. The county has received this award every year since 1983.

To earn the Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized CAFR whose contents conform to program standards and satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only. The current report continues to conform to the Certificate of Achievement program requirements, and is being submitted to GFOA to determine eligibility for another certificate.

The preparation of this report on a timely basis could not be accomplished without the efficient and dedicated service of our Chief Accountant, Jim Wahlstrom, and the entire Accounting Division of the Budget and Finance Department. We also wish to express our appreciation to all other county personnel for their assistance and cooperation during the year in implementing financial system enhancements. In particular, we wish to thank the County Executive and the County Council whose interest in, and support of, the financial obligations of *Pierce County* have significantly contributed to a quality financial operation.

Respectfully submitted,

A handwritten signature in black ink that reads "Patrick Kenney". The signature is written in a cursive style with a large initial "P".

Patrick Kenney
Director of Budget and Finance

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Pierce County
Washington

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
December 31, 2008

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

ELECTED OFFICIALS

December 31, 2009

COUNCIL:

| | |
|------------|----------------|
| District 1 | Shawn Bunney |
| District 2 | Joyce McDonald |
| District 3 | Roger Bush |
| District 4 | Tim Farrell |
| District 5 | Barbara Gelman |
| District 6 | Dick Muri |
| District 7 | Terry Lee |

COUNTY EXECUTIVE

Pat McCarthy

PROSECUTING ATTORNEY

Mark Lindquist

AUDITOR

Julie Anderson

ASSESSOR/TREASURER

Dale Washam

JUDICIAL:

Superior Court Judges:

| | |
|----------------------|-------------------------|
| Stephanie A. Arend | Linda CJ Lee |
| Rosanne Buckner | John A. McCarthy |
| Bryan E. Chushcoff | Kathryn J. Nelson |
| Ronald Culpepper | James Orlando |
| Frank E. Cuthbertson | Susan K. Serko |
| Thomas J. Felnagle | D. Gary Steiner |
| Frederick W. Fleming | Katherine M. Stolz |
| Beverly G. Grant | Brian Tollefson |
| John R. Hickman | Kitty-Ann van Doorninck |
| Vicki L. Hogan | Lisa Worswick |
| Thomas P. Larkin | |

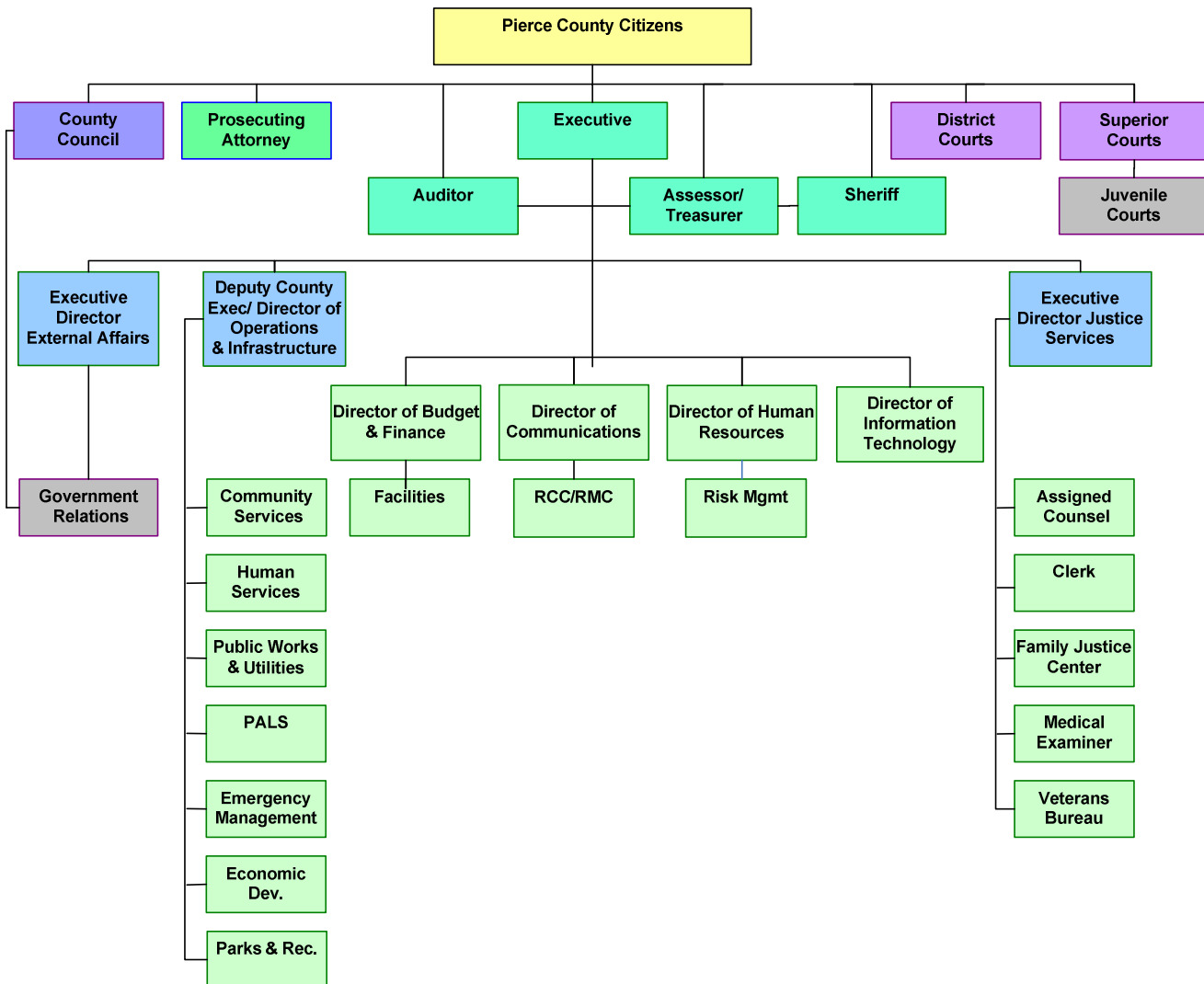
District Court Judges:

| | |
|-------------------|--------------------|
| Karla E. Buttorff | David M. Kenworthy |
| Franklin L. Dacca | Jack F. Nevin |
| James R. Heller | Pat O'Malley |
| Judy Rae Jasprica | Margaret Vail Ross |

ORGANIZATIONAL OVERVIEW

Pierce County 2009

Pierce County's home-rule charter was approved by the voters in November 1980 and became effective on May 1, 1981. The charter separated executive and legislative responsibilities by establishing the position of County Executive to serve as the chief executive officer and a seven-member Council to serve as the legislative branch.



The Council sets county policy and approves the annual budget. Council members are nominated and elected by the voters of seven districts in *Pierce County*. Legislative authority is exercised by the adoption and enactment of ordinances or resolutions. The executive branch is comprised of the Executive and all executive departments established by the Charter or by ordinance. Executive departments include three currently elected positions (Assessor/Treasurer, Auditor and Sheriff) with the other department directors recommended by the Executive and approved by the Council.