

RESOLUTION NO. 14-21

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF OAK HARBOR ESTABLISHING AN INVESTMENT POLICY.

WHEREAS, the City of Oak Harbor wishes to formally establish an Investment Policy; and

WHEREAS, the City of Oak Harbor wishes the Investment Policy be authorized by resolution of City Council;

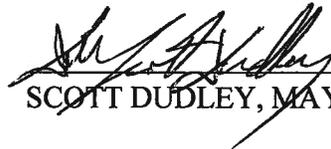
NOW THEREFORE, BE IT RESOLVED BY THE CITY COUNCIL OF THE CITY OF OAK HARBOR THAT:

Section 1. The City Council adopts the newly established Investment Policy as set forth in Attachment "A" to this Resolution.

Section 2. This Resolution, including the policy as shown in Attachment "A" shall become effective immediately upon its passage and approval.

PASSED by the City Council and approved by its Mayor this 3rd day of June, 2014.

THE CITY OF OAK HARBOR


SCOTT DUDLEY, MAYOR

Attest:

Approved as to Form:


Anna Thompson, City Clerk


Grant K. Weed, Interim City Attorney

Introduction:
Adopted:
Published:

ATTACHMENT A

 <p>City of Oak Harbor</p> <p>Finance Department</p>	Policy & Procedure Manual	
	Description:	No.
	Investment Policy	01
	Revision Date:	No.
	<i>April 23, 2014</i>	01

1. Policy Statement

It is the policy of the City of Oak Harbor to invest public funds in a manner which will provide maximum security with the highest investment return possible, while meeting the daily cash flow demands of the City and conforming to all Washington statutes governing the investment of public funds.

2. Scope

This investment policy applies to all financial assets of City of Oak Harbor. These funds are accounted for in City of Oak Harbor's Comprehensive Annual Financial Report which includes the following:

- General Fund
- Special Revenue Funds
- Debt Service Funds
- Capital Project Funds
- Enterprise Funds
- Internal Service Funds
- Trust and Agency Funds
- Any new fund/component unit created by the City Council, unless specifically exempted

3. Prudence

Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

The standard of prudence to be used by investment officials shall be the “prudent person” and/or “prudent investor” standard and shall be applied in the context of managing an overall portfolio. Investment officers acting in accordance with written procedures and the investment policy and exercising due diligence shall be relieved of personal responsibility for an individual security’s credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments.

In determining whether an investment official has exercised prudence with respect to an investment decision, the determination shall be made taking into consideration the investment of all funds over which the official had responsibility rather than a consideration as to the prudence of a single investment, a, whether the investment decision was consistent with the written policy of the entity.

4. **Objective**

The primary objectives, in priority order, of the City of Oak Harbor’s investment activities shall be:

- **Safety:** Safety of principal is the foremost objective of the investment program. Investments of the City of Oak Harbor shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. To attain this objective, diversification is required on order that potential losses on individual securities do not exceed the income generated from the remainder of the portfolio.
- **Liquidity:** The investment portfolio will remain sufficiently liquid to enable the City of Oak Harbor to meet all operating requirements which might be reasonably anticipated. This is accomplished by structuring the portfolio so that securities mature concurrent with cash needs to meet anticipated demands (static liquidity). Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets (dynamic liquidity).
- **Return on Investments:** The City of Oak Harbor’s investment portfolio shall be designed with the objective of attaining a market rate of return through budgetary and economic cycles, taking into account the City’s investment risk constraints and liquidity needs. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core of investment is limited to relatively low risk securities in anticipation of earning a fair rate of return relative to the risk being assumed. Securities shall generally be held until maturity with the following exceptions:
 - A security with declining credit may be sold early to minimize the loss of principal.

- A security swap would improve the quality, yield, or target duration of the portfolio.
- Liquidity needs of the portfolio require that the security be sold early.

5. Delegation of Authority

Management responsibility for the investment program is assigned to the Finance Director per OHMC 2.07.030. The Finance Director may delegate authority for the day-to-day administration, investing tracking, and reporting of the investment program to the Treasury Manager.

The Finance Director may also appoint an investment officer whose responsibilities will include initiating daily transactions in the investment portfolio based on liquidity and cash flow requirements of the city. In addition, the Finance Director shall establish written procedures for the operation of the investment program consistent with this investment policy.

Procedures should include reference to, if applicable: safekeeping, master repurchase agreements, wire transfer agreements, custody agreements and investment related banking services contracts. Such procedures shall include explicit delegation of authority to persons responsible for investment transactions.

No person may engage in an investment transaction except as provided under the terms of this policy without the express written consent of the Finance Director. The Finance Director shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

6. Investment Committee

The City of Oak Harbor shall establish an Investment Committee to act as an oversight body to the investment decisions of the Finance Director. The Investment Committee shall be comprised of two City Council members, the City Administrator, the Finance Director, and other interested stakeholders. The two City Council members and other interested stakeholders shall be appointed by the Mayor.

7. Ethics and Conflicts of Interest

Investment officials will recognize that the investment portfolio is subject to public review and evaluation. The overall program will be designed and managed with a degree of professionalism that is worth of the public trust.

Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with the proper execution of the investment program, or which could impair their ability to make impartial investment decisions. Employees and

investment officials shall disclose to the Mayor or City Administrator any material financial interests in financial institutions that conduct business within this jurisdiction, and they shall further disclose any personal financial/investment positions that could be related to the performance of City of Oak Harbor's portfolio. Employees and officers shall subordinate their personal investment transactions to those of City of Oak Harbor, particularly with regard to the timing of purchases and sales.

8. Authorized Financial Dealers and Institutions

Selection of a primary bank for the City of Oak Harbor for general banking services will be made by the Finance Director, per Oak Harbor Municipal Code Chapter 3.02.

The Finance Director will maintain a list of financial institutions authorized to provide investment services. In addition, a list will also be maintained of approved security broker/dealers selected by credit worthiness that are authorized to provide investment services in the State of Washington.

Authorized broker/dealers and financial institutions will be limited to those that meet one or more of the following:

- Financial institutions approved by the Washington Public Deposit Protection Commission (RCW 39.58); or,
- Primary dealers or regional dealers that qualify under SEC Rule 15C3-1 (uniform net capital rule); or,
- Non-primary dealers qualified under U.S. Securities and Exchange Commission Rule 15C3-1, the Uniform Net Capital Rule, and a certified member of the National Association of Securities Dealers.

As required by law (RCW 39.58), certificates of deposit will be purchased only from those institutions approved by the Washington Public Deposit Protection Commission (PDPC) as eligible for deposit of public funds. The Finance Director will annually adopt the eligibility list provided by the PDPC as the approved depository list.

The maximum amount placed with any one depository will not exceed the net worth of the institution as determined by the PDPC.

Qualified broker/dealers and financial institution will be reviewed and selected by the Finance Director on a routine basis. All broker/dealers and financial institutions who desire to do business with the City of Oak Harbor must provide the Finance Director with the following:

- Annual audited financial statements.
- Proof of Financial Industry Regulation Authority (FINRA) certification.
- Proof of registration with the State of Washington.

- A completed Broker/Dealer questionnaire and a certification of having read the City of Oak Harbor's Investment Policy.

The Finance Director will conduct an annual review of the financial condition of the firms. A current audited financial statement is required to be on file for each financial institution and broker/dealer with whom the City invests.

Authorized Financial Dealers and Institutions currently authorized to provide investment services to the city are:

- All Financial Institutions approved by the Washington Public Deposit Protection Commission (RCW 39.58). Doug Extine, Deputy State Treasurer, 360-902-9012.
- Piper Jaffray & Co/Seattle Northwest Securities Corporation, Mark Rodgers, 206-628-5452.
- Time Value Investments (TVI), Paul Jarvis, Managing Director, 206-365-3003.

The Finance Director is authorized to remove any Broker/Dealer, without approval by the investment committee, for recommending investments outside of the scope of the City's investment policy or the laws and regulations pertaining to municipal investments. Upon removal of a Broker/Dealer, the Director of Finance shall provide the members of the investment Committee and the Mayor a written report as to the reason of the removal. Broker/Dealers removed by the Finance Director may appeal his decision by forwarding a written appeal to the City Administrator.

9. Authorized and Suitable Investments

From the governing body perspective, special care must be taken to ensure that the list of instruments includes only those allowed by law and those that local investment managers are trained and competent to handle.

The City of Oak Harbor is empowered by statute to invest in securities and investments authorized by state statute as defined in RCW's 39.58 and 39.59. Authorized investments include:

- U.S. Treasury Obligations.
- Non-negotiable Certificates of Deposit of financial institutions which are qualified public depositories as defined by RCW 39.58.010(2) and in accordance with the restrictions therein.
- U.S. Government Agency obligations and U.S. Government Sponsored Enterprises (GSE's) which may include, but are not limited to the following: Federal Home Loan Bank (FHLB), Federal Farm Credit Bank (FFCB), Government National Mortgage

Association (GNMA), Federal Home Loan Mortgage Corporation (FHLMC), and Federal National Mortgage Association (FNMA), Student Loan Marketing Corporation (SLMA).

- Bankers' Acceptances (BA's) purchased through State of Washington Financial Institutions and authorized broker/dealers. Banker's Acceptances shall not be longer than six months duration. Investments in Banker's Acceptances must be in the top 30 banks in the United States, including all banks in the State of Washington as authorized by the Public Deposit Protection Commission. Further, within these limitations, investments may be made only in those banks whose other negotiable obligations are rated at least A-1, P-1, or F-1 (at the time of purchase) by at least two or more internationally recognized rating agencies such as Moody's or Standard and Poors.
- Bonds of the State of Washington and any local government in the State of Washington which have, at the time of investment, one of the three highest credit ratings of a nationally recognized rating agency.
- General obligation bonds of a state other than the State of Washington and general obligation bonds of a local government of a state other than the State of Washington, which bonds have at the time of investment one of the three highest credit ratings of a nationally recognized rating agency.
- Repurchase agreements provided that a signed Master Repurchase Agreement shall be on file in the City of Oak Harbor's Finance Office for all financial institution that enter into a repurchase agreement with the City. All repurchase agreements will be collateralized at a minimum of 102% of market value of principal and interest. The only eligible collateral for repurchase agreement will be direct obligations of the U.S. Treasury, U.S. Government Agency and/or U.S. Government instrumentality obligations. All obligations will be held in third party safekeeping. Third party safekeeping agreements must be entered into with a signed agreement between the safekeeping financial institution and the City of Oak Harbor Finance Director. All securities in a repurchase agreement shall be priced daily to reflect current market conditions for both principal and accrued interest. Securities shall be purchased from either primary dealers or from institutions that are members of the Washington Public Depository. Credit worthiness of the institution will also be considered.

A signed master repurchase agreement in conformance with the Public Securities Association (PSA) model agreement and supplemented with the Finance Director's policy on repurchase agreements must be executed prior to entering into a repurchase agreement transaction.

- Collateral will always be held by an independent third party with whom City of Oak Harbor has a current custodial agreement. A clearly marked evidence of ownership must be supplied to City of Oak Harbor and retained. The right of substitution is granted only upon approval of City of Oak Harbor.

- Washington State Local Government Investment Pool (LGIP). The Finance Director will keep on file the most recent LGIP Investment Policy and operations manual. This policy will be assessed for safety of funds on deposit with the LGIP and risks associated with investment strategies. In addition, the LGIP will complete a questionnaire for the Finance Director which will include the following:
 - A description of eligible securities.
 - How interest and fees are calculated.
 - How gains and losses are calculated.
 - A description of how the securities are safeguarded.
 - How often the securities are priced.
 - How often the program is audited.
 - Deposit and withdrawal restrictions.
 - Information on how bond proceeds are accounted for in the LGIP.
- Commercial Paper purchased in the secondary market and complying with the State Investment Board requirements. These requirements include commercial paper rated at least A-1, P-1, or F-1 (at the time of purchase) by at least two (2) nationally recognized agencies such as Moody's and Standard and Poors and have a maturity not exceeding 180 days. Maturities in excess of 100 days must also have a long-term rating of Aa or better by at least one recognized rating agency.
- Mutual funds used specifically for debt issues related to arbitrage.
- Other investments authorized by law.

10. Collateralization:

Repurchase agreements:

- The collateral for repurchase agreements shall be U.S. Treasury or Agency securities with a term of maturity not to exceed the maximum maturity allowed by the investment policy.
- Mortgage-backed securities of any maturity will not be accepted as collateral.
- In order to anticipate market changes and provide a level of security for all funds, the collateralization level will be at 102% of market value of principal and accrued interest.
- Collateral to be delivered to and held by the trust department of the bank with whom the Finance Director is currently using as the City's safekeeping custodian.
- At a minimum, the value of the securities must be marked to market on a weekly basis. Prevailing market conditions may dictate more frequent repricing at the discretion of the Finance Director.

11. Diversification:

It is the policy of the City of Oak Harbor to diversify its investment portfolio. To eliminate the

risk of loss resulting from the over-concentration of assets in a specific maturity, issuer, or class of securities, all cash and cash equivalent assets in all funds shall be diversified by maturity, issuer, and by class of security. Diversification strategies shall be determined and revised periodically by the Finance Director for all funds. IN establishing specific diversification strategies, the following constraints shall apply:

<u>Type of Security</u>	<u>Maximum Holdings</u>
Certificates of Deposit	40% of Portfolio
U.S. Treasury Obligations	100% of Portfolio
Federal Agency Securities	90% of Portfolio
Bankers Acceptances	25% of Portfolio
Bonds of the State of Washington or any local government in the State of Washington	20% of Portfolio 10% per Issuer
Bonds of other states or local governments of a state other than the State of Washington	15% of Portfolio 10% per Issuer
Municipal Investment Accounts	40% of Portfolio
Repurchase Agreements	40% of Portfolio 10% per Dealer
Washington State Local Government Investment Pool	100% of Portfolio
Commercial Paper	10% of Portfolio
Mutual Funds	Arbitrage Related Only

12. Sale of Portfolio

Any major changes in the Investment Strategy including the liquidation of the portfolio shall require a majority vote by the City Council.

13. Safekeeping and Custody:

- **Delivery vs. Payment** - All security transactions, including collateral for repurchase agreements, entered into by the City of Oak Harbor will be conducted on a delivery-versus-payment (DVP) basis and will be evidenced by safekeeping receipts to ensure that securities are deposited with a third party custodian prior to the release of funds.
- **Safekeeping** - Securities will be held by an independent third party custodian designated by the Finance Director.
- **CD's** - Certificates of Deposit in the City's name will be delivered to and held in the Finance Department.

14. Maturities

To the extent possible and to preclude the sales of securities that could result in a loss, the City of Oak Harbor will attempt to match its investments with anticipated cash flow requirements. Because of inherent difficulties in accurately forecasting cash flow requirements, a portion of the portfolio should be continuously invested in readily available funds such as the Washington State Local Government Investment Pool or money market funds to ensure that appropriate liquidity is maintained to meet ongoing obligations. To this extent, 20% of the portfolio, at the time of investment, will be comprised of investments maturing within one year.

Unless matched to a specific cash flow or restricted by state guidelines, the City will directly invest remaining funds in authorized securities not to exceed five years in maturity except when compatible with a specific fund’s investment needs. For example, reserve funds may be invested in securities exceeding five years if the maturity of such investments is made to coincide as nearly as practical with the expected use of the funds.

To ensure additional liquidity and to provide for ongoing market opportunity the weighted average maturity and modified duration of the overall portfolio shall not exceed two years without the prior written approval of the Finance Director. Additional, more restrictive guidelines may be adopted at the discretion of the Finance Director.

Within confines of the diversification limits, the following investment decision amount and maturity limits are established:

<u>Maturity</u>	<u>Individual Investment Size</u>	<u>Authorization Required</u>
Overnight collateral	Unlimited	Finance Director
Less than one year	Up to \$2,000,000 par value	Finance Director
More Than One Year		
Less Than Three years	Up to \$2,000,000 par value	Finance Director
More than Three Years		
Less Than Five Years	Up to \$2,000,000 par value	Finance Director & Investment Committee

15. Internal Control

The investment officer is responsible for establishing and maintaining an internal control structure designed to ensure that the assets are protected from loss, theft, or misuse. The Finance Director shall establish an annual process of independent review by an external auditor. This review will provide internal control by assuring compliance with policies and procedures. The internal controls shall address the following points:

- Control or collusion.
- Separation of transaction authority from accounting and recordkeeping.

- Custodial Safekeeping.
- Avoidance of physical delivery securities.
- Clear delegation of authority to subordinate staff members.
- Written confirmation of transactions for investments and wire transfers.
- Development of a wire transfer agreement with the lead bank and third-party custodian.

16. Performance Standards

The investment portfolio will be managed in accordance with the parameters specified within this policy. The investment portfolio will be designed to obtain an average rate of return during budgetary and economic cycles, consistent with the investment objectives and cash flow needs. A series of appropriate benchmarks shall be established against which performance shall be compared on a regular basis. The benchmarks will be reflective of the actual securities being purchased and the risks undertaken. The benchmarks will have a similarly weighted average maturity as the portfolio.

Accordingly, the City of Oak Harbor's investment portfolio will be designed to obtain an average rate of return which meets or exceeds the six month Treasury, the average Fed Funds rate, and the annual rate paid by the Washington State Local Government Investment Pool.

17. Procedures

Day-to-day procedures concerning investment management and accounting are outside the scope of this policy. As deemed necessary, the Finance Director will establish written procedures for the operation of the investment program consistent with this policy.

18. Reporting:

The Finance Director shall provide the Investment Committee quarterly investment reports which provide an accurate and meaningful summary of the current position of the portfolio for the City of Oak Harbor. The Finance Director shall report to the Investment Committee the current investment strategy being followed and recent economic conditions and market developments which have a bearing on this strategy. This report will be prepared in a manner which will allow the Investment Committee to ascertain whether investment activities during the reporting period have conformed to the investment policy. The report will include:

- A listing of individual securities held at the end of the reporting period by authorized investment category or type.
- Asset allocation of types of securities.
- Performance of portfolio and its appropriate benchmarks.

The investment report may include other pertinent information as requested.

19. Investment Policy Adoption

The City of Oak Harbor's investment policy will be adopted by resolution of the City Council. The policy will be reviewed on an annual basis by the Investment Committee with approval being made on any modifications. Upon adoption, the City will submit the Investment Policy to the Washington Public Treasurers Association for certification.

Glossary of Terms

The following is a glossary of key investing terms, many of which appear in the City of Oak Harbor Investment Policy:

Agency - A debt security issued by a federal or federally sponsored agency. Federal agencies are backed by the full faith and credit of the U.S. Government. Federally sponsored agencies (FSAs) are backed by each particular agency with a market perception that there is an implicit government guarantee. An example of a federal agency is the Government National Mortgage Association (GNMA). An example of an FSA is the Federal National Mortgage Association (FNMA).

Amortization - The systematic reduction of the amount owed on a debt issue through periodic payments of principal.

Average Maturity - The average length of time that an issue of serial bonds and/or term bonds with a mandatory sinking fund feature is expected to be outstanding.

Bankers' Acceptance (BA) - A draft or bill of exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the issuer.

Basis Point - A unit of measurement used in the valuation of fixed-income securities equal to 1/100 of 1 percent of yield, e.g., "1/4" of 1 percent is equal to 25 basis points.

Bid - The indicated price at which a buyer is willing to purchase a security or commodity.

Bond - A long-term debt security, or IOU, issued by a government or corporation that generally pays a stated rate of interest and returns the face value on the maturity date.

Book Value - The value at which a security is carried on the inventory lists or other financial records of an investor. The book value may differ significantly from the security's current value in the market.

Broker - A broker brings buyers and sellers together for a commission paid by the initiator of the transaction or by both sides; he does not position. In the money market, brokers are active in markets in which banks buy and sell money and in interdealer markets.

Callable Bond - A bond issue in which all or part of its outstanding principal amount may be redeemed before maturity by the issuer under specified conditions.

Call Price - The price at which an issuer may redeem a bond prior to maturity. The price is usually at a slight premium to the bond's original issue price to compensate the holder for loss of income and ownership.

Call Risk - The risk to a bondholder that a bond may be redeemed prior to maturity.

Cash Sale/Purchase - A transaction which calls for delivery and payment of securities on the same day that the transaction is initiated.

Certificate of Deposit (CD) - A time deposit with a specific maturity evidenced by a certificate. Large-denomination CDs are typically negotiable.

Collateral - Securities, evidence of deposit or other property which a borrower pledges to secure repayment of a loan. Also refers to securities pledged by a bank to secure deposits of public monies.

Commercial Paper - An unsecured short-term promissory note issued by corporations, with maturities ranging from 2 to 270 days.

Convexity - A measure of a bond's price sensitivity to changing interest rates. A high convexity indicates greater sensitivity of a bond's price to interest rate changes.

Coupon Rate - The annual rate of interest received by an investor from the issuer of certain types of fixed-income securities (also known as the "interest rate").

Credit Quality - The measurement of the financial strength of a bond issuer. This measurement helps an investor to understand an issuer's ability to make timely interest payments and repay the loan principal upon maturity. Generally, the higher the credit quality of a bond issuer, the lower the interest rate paid by the issuer because the risk of default is lower. Credit quality ratings are provided by nationally recognized rating agencies.

Credit Risk - The risk to an investor that an issuer will default in the payment of interest and/or principal on a security.

Current Yield (Current Return) - A yield calculation determined by dividing the annual interest received on a security by the current market price of that security.

Custodian – An independent third party that holds securities in safekeeping as an agent for the City.

Dealer - A dealer, as opposed to a broker, acts as a principal in all transactions, buying and selling for his own account.

Delivery Versus Payment (DVP) - A type of securities transaction in which the purchaser pays

for the securities when they are delivered either to the purchaser or his/her custodian.

Depository Bank – A local bank used as the point of deposits for cash receipts.

Derivative Security - Financial instrument created from, or whose value depends upon, one or more underlying assets or indexes of asset values.

Discount - The difference between the cost price of security and its value at maturity when quoted at lower than face value. A security selling below original offering price shortly after sale is also considered to be at a discount.

Discount Securities - Non-interest bearing money market instruments that are issued at a discount and redeemed at maturity for full face value, e.g., U.S. Treasury bills.

Diversification -A process of investing assets among range of security types by sector, maturity, and quality rating.

Duration - A measure of the timing of the cash flows, such as the interest payment and Principal payment, to be received from a given fixed-income security. This calculation is based on three variables: term to maturity, coupon rate, and yield to maturity. The duration of a security is a useful indicator of its price volatility for given changes in interest rates.

Fair Value - The amount at which an investment could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

Federal Credit Agencies -Agencies of the Federal government set up to supply credit to various classes of institutions and individuals, e.g., S&Ls, small business firms, students, farmers, farm cooperatives, and exporters.

Federal Deposit Insurance Corporation (FDIC) - A federal agency that insures bank deposits, currently up to \$250,000 per deposit.

Federal Funds (Fed Funds) - Funds placed in Federal Reserve banks by depository institutions in excess of current reserve requirements. These depository institutions may lend fed funds to each other overnight or on a longer basis. They may also transfer funds among each other on a same-day basis through the Federal Reserve banking system. Fed funds are considered to be immediately available funds.

Federal Home Loan Banks (FHLB) - The institutions that regulate and lend to savings and loan associations. The Federal Home Loan Banks play a role analogous to that played by the Federal Reserve Banks vis-a-vis member commercial banks.

Federal National Mortgage Association (FNMA or Fannie Mae) - FNMA, like GNMA, was chartered under the Federal National Mortgage Association Act in 1938. FNMA is a federal corporation working under the auspices of the Department of Housing and Urban

Development, H.U.D. It is the largest single provider of residential mortgage funds in the United States. Fannie Mae, as the corporation is called, is a private stockholder-owned corporation. The corporation's purchases include a variety of adjustable mortgages and second loans in addition to fixed-rate mortgages. FNMA's securities are also highly liquid and are widely accepted. FNMA assumes and guarantees that all security holders will receive timely payment of principal and interest.

Federal Open Market Committee (FOMC) - Consists of seven members of the Federal Reserve Board and five of the twelve Federal Reserve Bank Presidents. The President of the New York Federal Reserve Bank is a permanent member while the other Presidents serve on a rotating basis. The Committee periodically meets to set Federal Reserve guidelines regarding purchases and sales of Government Securities in the open market as a means of influencing the volume of bank credit and money.

Federal Reserve System - The central bank of the United States created by Congress and consisting of a seven member Board of Governors in Washington, D.C., 12 regional banks and about 5,700 commercial banks that are members of the system.

Fiscal Agency – A financial institution that handles certain bond and coupon redemptions on behalf of an investor.

Government National Mortgage Association (GNMA or Ginnie Mae) - Securities Guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loan associations, and other financial institutions. Security holder is protected by the full faith and credit of the U.S. Government. Ginnie Mae securities are backed by FHA, VA, or FMHM mortgages. The term pass-through is often used to describe Ginnie Maes.

Government Securities - An obligation of the U.S. government, backed by the full faith and credit of the government. These securities are regarded as the highest quality of investment securities available in the U.S. securities market. See "Treasury Bill, Notes, and Bonds."

Interest Rate - See "Coupon Rate".

Interest Rate Risk - The risk associated with declines or rises in interest rates which cause an investment in a fixed-income security to increase or decrease in value.

Internal Controls -An internal control structure designed to ensure that the assets of the entity are protected from loss, theft, or misuse. The internal control structure is designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that 1) the cost of a control should not exceed the benefits likely to be derived; and 2) the valuation of costs and benefits requires estimates and judgments by management. Internal controls should address the following points:

- 1. Control of collusion** - Collusion is a situation where two or more employees are

working in conjunction to defraud their employer.

2. Separation of transaction authority from accounting and record keeping – By separating the person who authorizes or performs the transaction from the people who record or otherwise account for the transaction, a separation of duties is achieved.

3. Custodial safekeeping - Securities purchased from any bank or dealer including appropriate collateral (as defined by state law) shall be placed with an independent third party for custodial safekeeping.

4. Avoidance of physical delivery securities - Book-entry securities are much easier to transfer and account for since actual delivery of a document never takes place. Delivered securities must be properly safeguarded against loss or destruction. The potential for fraud and loss increases with physically delivered securities.

5. Clear delegation of authority to subordinate staff members - Subordinate staff members must have a clear understanding of their authority and responsibilities to avoid improper actions. Clear delegation of authority also preserves the internal control structure that is contingent on the various staff positions and their respective responsibilities.

6. Written confirmation of transactions for investments and wire transfers - Due to the potential for error and improprieties arising from telephone and electronic transactions, all transactions should be supported by written communications and approved by the appropriate person. Written communications may be via fax if on letterhead and if the safekeeping institution has a list of authorized signatures.

7. Development of a wire transfer agreement with the lead bank and third-party custodian - The designated official should ensure that an agreement will be entered into and will address the following points: controls, security provisions, and responsibilities of each party making and receiving wire transfers

Inverted Yield Curve -A chart formation that illustrates long-term securities having lower yields than short-term securities. This configuration usually occurs during periods of high inflation coupled with low levels of confidence in the economy and a restrictive monetary policy.

Investment Company Act of 1940 - Federal legislation which sets the standards by which investment companies, such as mutual funds, are regulated in the areas of advertising, promotion, performance reporting requirements, and securities valuations.

Investment Policy - A concise and clear statement of the objectives and parameters formulated by an investor or investment manager for a portfolio of investment securities.

Investment-grade Obligations - An investment instrument suitable for purchase by institutional investors under the prudent person rule. Investment-grade is restricted to those obligations rated BBB or higher by a rating agency.

Liquidity -A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value. In the money market, a security is said to be liquid if the spread between bid and asked price is narrow and reasonable size can be done at those quotes.

Local Government Investment Pool (LGIP) - The aggregate of all funds from political subdivisions that are placed in the custody of the State Treasurer for investment and reinvestment.

Mark to Market – An adjustment in the valuation of a securities portfolio to reflect the current market values of the respective securities in the portfolio. This process is also used to ensure that margin accounts are in compliance with maintenance.

Market Risk - The risk that the value of a security will raise or decline as a result of changes in market conditions.

Market Value - The price at which a security is trading and could presumably be purchased or sold.

Master Repurchase Agreement - A written contract covering all future transactions between the parties to repurchase-reverse repurchase agreements that establish each party's rights in the transactions. A master agreement will often specify, among other things, the right of the buyer-lender to liquidate the underlying securities in the event of default by the seller-borrower.

Maturity - The date upon which the principal or stated value of an investment becomes due and payable.

Money Market - The market in which short-term debt instruments (bills, commercial paper, bankers' acceptances, etc.) are issued and traded.

Open Market Operations - Purchases and sales of government and certain other securities in the open market by the New York Federal Reserve Bank as directed by the FOMC in order to influence the volume of money and credit in the economy. Purchases inject reserves into the bank system and stimulate growth of money and credit; sales have the opposite effect. Open market operations are the Federal Reserve's most important and most flexible monetary policy tool.

National Association of Securities Dealers (NASD) - A self-regulatory organization (SRO) of brokers and dealers in the over-the-counter securities business. It's regulatory mandate includes authority over firms that distribute mutual fund shares as well as other securities.

Net Asset Value - The market value of one share of an investment company, such as a mutual fund. This figure is calculated by totaling a fund's assets which includes securities, cash, and any accrued earnings, subtracting this from the fund's liabilities and dividing this total by the number of shares outstanding. This is calculated once a day based on the closing price for each security in the fund's portfolio (See below). $(\text{Total assets}) - (\text{Liabilities}) / (\text{Number of shares outstanding})$.

Nominal Yield - The stated rate of interest that a bond pays its current owner, based on par value of the security. It is also known as the "coupon", "coupon rate", or "interest rate".

Offer - An indicated price at which market participants are willing to sell a security or commodity. Also referred to as the "ask price".

Par - Face value or principal value of a bond, typically \$1,000 per bond.

Portfolio - Collection of securities held by an investor.

Positive Yield Curve - A chart formation that illustrates short-term securities having lower yields than long-term securities.

Premium - The amount by which the price paid for a security exceeds the security's par-value.

Primary Dealer - A group of government securities dealers that submit daily reports of market activity and positions and monthly financial statements to the Federal Reserve Bank of New York and are subject to its informal oversight. Primary dealers include Securities and Exchange Commission (SEC) registered securities broker-dealers, banks, and a few unregulated firms.

Prime Rate - A preferred interest rate charged by commercial banks to their most creditworthy customers. Many interest rates are keyed to this rate.

Principal - The face value or par value of a debt instrument. Also may refer to the amount of capital invested in a given security.

Prudent Person Rule - An investment standard outlining the fiduciary responsibilities of public funds-investors-relating-to investment practices.

Qualified Public Depositories - A financial institution which does not claim exemption from the payment of any sales or compensating use or ad valorem taxes under the laws of this state, which has segregated for the benefit of the commission eligible collateral having a value of not less than its maximum liability and which has been approved by the Public Deposit Protection Commission to hold public deposits.

Rate of Return - The yield obtainable on a security based on its purchase price or its current market price. This may be the amortized yield to maturity on a bond or the current income

return.

Repurchase Agreement (RP or REPO) - A holder of securities sells these securities to an investor with an agreement to repurchase them at a fixed price on a fixed date. The security "buyer" in effect lends the "seller" money for the period of the agreement, and the terms of the agreement are structured to compensate him for this. Dealers use RP extensively to finance their positions. Exception: When the Fed is said to be doing RP, it is lending money, that is, increasing bank reserves.

Reverse Repurchase Agreement (Reverse Repo) - An agreement of one party to purchase securities at a specified price from a second party and a simultaneous agreement by the first party to resell the securities at a specified price to the second party on demand or at a specified date.

Safekeeping - A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank's vaults for protection.

Secondary Market - A market made for the purchase and sale of outstanding issues following the initial distribution.

Securities & Exchange Commission - Agency created by Congress to protect investors in securities transactions by administering securities legislation.

Swap - Trading one asset for another.

Term Bond - Bonds comprising a large part or all of a particular issue which come due in a single maturity. The issuer usually agrees to make periodic payments into a sinking fund for mandatory redemption of term bonds before maturity.

Total Return - The sum of all investment income plus changes in the capital value of the portfolio. For mutual funds, return on an investment is composed of share price appreciation plus any realized dividends or capital gains. This is calculated by taking the following components during a certain time period. $(\text{Price Appreciation}) + (\text{Dividends paid}) + (\text{Capital Gains}) = \text{Total Return}$

Treasury Bills - Short-term U.S. government non-interest bearing debt securities with maturities of no longer than one year and issued in minimum denominations of \$10,000. Auctions of three and six month bills are weekly, while auctions of one-year bills are monthly. The yields on these bills are monitored closely in the money markets for signs of interest rate trends.

Treasury Bonds - Long-term U.S. government debt securities with maturities of ten years or longer and issued in minimum denominations of \$1,000. Currently, the longest outstanding maturity for such securities is 30 years.

Treasury Notes - Intermediate U.S. government debt securities with maturities of one to 10 years and issued in denominations ranging from \$1,000 to \$1 million or more.

Uniform Net Capital Rule - SEC Rule 15C3-1 outlining capital requirements for broker/dealers.

Volatility - A degree of fluctuation in the price and valuation of securities.

Weighted Average Maturity (WAM) - The average maturity of all the securities that comprise a portfolio. According to SEC rule 2A-7, the WAM for SEC registered money market mutual funds may not exceed 90 days and no one security may have a maturity that exceeds 397 days.

Yield - The current rate of return on an investment security generally expressed as a percentage of the security's current price.

Yield Curve - A graphic representation that depicts the relationship at a given point in time between yields and maturity for bonds that are identical in every way except maturity. A normal yield curve may be alternatively referred to as a positive yield curve.

Yield-to-call (YTC) - The rate of return an investor earns from a bond assuming the bond is redeemed (called) prior to its nominal maturity date.

Yield-to-maturity - The rate of return yielded by a debt security held to maturity when both interest payments and the investor's potential capital gain or loss are included in the calculation of return.

Zero-coupon Securities - Security that is issued at a discount and makes no periodic interest payments. The rate of return consists of a gradual accretion of the principal of the security and is payable at par upon maturity.