
City of Port Angeles



Investment Policy

December 6, 2011

1. Purpose

The purpose of this document is to identify various policies and procedures that enhance opportunities for a prudent and systematic investment policy and to organize and formalize investment-related activities.

The policy outlines investments scope, objectives, delegation of authority, reporting requirements, internal control, investment limitations, safeguarding requirements, liquidity, performance expectation, quality, and maturity.

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

2. Scope

It shall be the general policy of the City of Port Angeles to pool all available cash into a common investment portfolio as authorized by RCW 35A.40.050.

The investment policy applies to all financial assets of the City of Port Angeles ("City"). These funds are accounted for in the City's Financial Reports and include all funds:

- *General Fund*
- *Special Revenue Funds*
- *Capital Project Funds*
- *Enterprise Funds*
- *Trust and Agency Funds*
- *Retirement/Pension Funds*
- *Any new funds created by Council*

3. Objective

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

3.1 Safety

Safety of principal is the foremost objective. It is the primary duty and responsibility of the City Treasurer to protect, preserve, and maintain cash and investments placed in his/her trust on behalf of the citizens of the community.

Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk and interest rate risk.

a. Credit Risk - The City of Port Angeles will minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

- Limiting investments to the safest types of securities.
- Pre-qualifying the financial institutions, brokers/dealers, intermediaries,

and advisers with which the City will do business.

- Diversify the investment portfolio so that potential losses on individual securities will be minimized.

b. Interest Rate Risk - The City will minimize the risk that the market value of securities in the portfolio will fall due to changes in general interest rates, by:

- Structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity.
- Investing operating funds primarily in shorter-term securities, money market mutual funds, or similar investment pools.

3.2 Liquidity

The City's investment portfolio shall remain sufficiently liquid to enable the City to meet all operating requirements which might be reasonably anticipated. Because all cash requirements cannot be anticipated, investments in securities with active secondary or resale markets are recommended. A portion of the portfolio also may be placed in money market mutual funds or local government investment pools which offer same day liquidity for short-term funds.

3.3 Return on Investment (Yield)

Yield should become a consideration only after the basic requirements of safety and liquidity have been met. The City's investment portfolio shall be managed in a manner to attain a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. The core of investments are limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed. Securities shall not be sold prior to maturity with the following exceptions:

- a. A security with declining credit may be sold early to minimize loss of principal.
- b. A security swap would improve the quality, yield, or target duration in the portfolio.
- c. Liquidity needs of the portfolio require that the security be sold.

4. Prudence

The standard of prudence to be applied by investment officials shall be the "prudent investor" rule, which states "...investments shall be made with judgement 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 Investment officer, acting in accordance with written procedures 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 development.

5. Delegation of Authority

Authority for investment decisions shall be granted to the City Manager, Finance Director and City Treasurer.. Each is authorized to sign necessary agreements and documents for the purpose of carrying out this policy which do not obligate the City for the expenditure of funds.

Management responsibility for the investment program is hereby delegated to the Finance Director and/or City Treasurer.

The City Treasurer or Finance Director shall be responsible for managing the day-to-day operation of the portfolio. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the City Treasurer and adopted by the City Council.

Procedures should include reference to: Safekeeping, delivery vs payment, investment accounting, repurchase agreements, wire transfer agreements, and collateral/depository agreements. The City Treasurer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinates.

6. Ethics and Conflicts of Interest

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

- 6.1** Employees and investment officials authorized to place or approve investments shall not personally, nor through a close relative, maintain any accounts, interest, or private dealings with any firm with which the City places investments, except for regular savings accounts, checking accounts, money market accounts, or other similar transactions which are offered on a non-negotiable basis to the general public.
- 6.2** All persons authorized or approved for investments shall disclose to the City Manager any material financial interest in financial institutions that conduct business within this jurisdiction.
- 6.3** All personnel involved in the investment function shall adhere closely to the City's Code of Ethics.

7. Authorized Financial Dealers and Institutions

The City Treasurer will maintain a list of financial institutions. As required by the Public Deposit Protection Commission (PDPC) all authorized public depositories will be located

in the State of Washington (RCW 39.58.080).

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; or
- primary dealers recognized by the Federal Reserve Bank; or
- non-primary dealers or institutions 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.

- 7.1 Whenever possible, the City shall make an effort to utilize brokers or dealers doing business in the State of Washington, or recognized adequately capitalized dealers on the west coast.
- 7.2 A current audited financial statement is required to be on file for each financial institution and broker/dealer in which the City invests.
- 7.3 In selecting financial institutions for the deposit or investment of City funds, the Treasurer shall continue to monitor the financial institutions' credit characteristics and financial history throughout the period in which City funds are deposited or invested.

8. Authorized Investments

All municipal corporations in Washington State, including the City of Port Angeles, are empowered by statute to invest in the following types of securities. Eligible investments are only those securities and deposits authorized by State statute as defined in RCW 39.58 and 39.59.

For the City of Port Angeles, the following securities are authorized investments:

- 8.1 Investment deposits, including certificates of deposit, with qualified public depositories as defined in RCW 39.58.
- 8.2 Certificates, notes, or bonds of the United States, or other obligations of the United States or its agencies, or of any corporation wholly owned by the government of the United States (such as the Government National Mortgage Association).
- 8.3 Obligations of government-sponsored corporations which are eligible as collateral for advances to member banks as determined by the Board of Governors of the Federal Reserve System. (These include, but are not limited to, Federal Home Loan Bank notes and bonds, Federal Farm Credit Bank consolidated notes and bonds, and Federal National Mortgage Association notes, bonds and guaranteed certificates of participation).
- 8.4 Bankers' acceptances purchased on the secondary market.
- 8.5 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.

- 8.6 Repurchase agreements for securities listed in 2, 3, and 4 above, provided that the transaction is structured so that the City of Port Angeles obtains control over the underlying securities and a Master Repurchase Agreement has been signed with the bank or dealer.
- 8.7 State of Washington Investment Pool.
- 8.8 Commercial Paper purchased in the secondary market and having received the highest rating by at least two (2) Nationally Recognized Statistical Rating Organization (NRSROs) at the time of purchase and adhering to the investment policies and procedures adopted by the State Investment Board.
- 8.9 Mutual funds used specifically for debt issues related to arbitrage.

9. Safekeeping and Custody

The City recognizes that investment risks can result from issuer defaults, market price changes or various technical complications leading to temporary illiquidity.

To decrease the risk of default, the City Treasurer shall periodically establish guidelines and strategies for investment.

In addition to general policy consideration, the following specific policies shall be implemented.

- 9.1 All security transactions, including collateral for repurchase agreements, entered into by the City of Port Angeles shall be conducted on a delivery-versus-payment (DVP) basis. Securities purchased by the entity will be delivered against payment and held in a custodial safekeeping account with the trust department of a bank. The trust department of a bank, a third party custodian, will be designated by the Investment Committee and all transactions will be evidenced by safekeeping records.
- 9.2 To protect against potential fraud and embezzlement, bearer instruments shall be secured through third-party custody and safekeeping procedures provided by a financial institution designated as primary agent. The primary agent shall issue a safekeeping receipt to the City of Port Angeles listing the specific instrument, rate, maturity and all other pertinent information.
- 9.3 Purchases of Bankers' Acceptances shall be limited to the top 25 national banks and the top six national banks chartered to do business in the State of Washington. Acceptances from highly rated foreign banks should be in the top 100 world banks.
- 9.4 For purchasing certificates of deposit (CDs) the City's investments should be limited to 85% of net worth of such institution. The Institution's status shall be reviewed and accepted by the Public Deposit Protection Commission (PDPC) or properly collateralized as required by the state for

amounts exceeding FDIC and FSLIC coverage.

10. Diversification

It is the policy of Port Angeles to diversify its investment portfolios. To eliminate 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 the class of security. Diversification strategies shall be determined and revised periodically by the Finance Director and investment officer for all funds. In establishing specific diversification strategies, the following constraints shall apply:

Maximum % of Portfolio

Washington State Local Government Investment Pool - 100%

U.S. Treasury Obligations – 100%

Federal Agency securities – 100%

Municipal Investment Accounts – 40%

Certificates of Deposit (CDs) - 50%

Repurchase Agreements (Repos) - 40%

Bonds of State of Washington or any local government in the State of Washington – 20%

Bonds of other states or local governments of a state other than the State of Washington - 15%

11. Maturities

To the extent possible and to preclude sales of securities that could result in a loss, investments will be made to coincide 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 Local Government Investment Pool and money market funds to ensure that appropriate liquidity is maintained to meet ongoing obligations.

- 11.1 To this extent, 10% of the portfolio, at the time of investment, will be comprised of investments maturing within a year.
- 11.2 Satisfying this requirement, remaining funds may be invested in authorized securities not to exceed five and a half years in maturity, except when compatible with a specific fund's investment needs. Maturities longer than five and a half years must have the prior written approval of the Treasurer.
- 11.3 To ensure additional liquidity and provide for ongoing market opportunity, the weighted average maturity and effective duration of the overall portfolio shall not exceed three years without the prior written approval of the Treasurer.

12. Selection of Investment Instruments

Investments shall be placed using an informal bidding procedure where rates will be received from at least three institutions. With the following exception, the investment will be placed with the highest bidder. In order to stimulate the local economy, the City may place an investment with a local institution that is not the highest bidder, provided that the bid is not more than 25 basis points below the highest bidder. A local institution is defined as a bank or savings and loan association doing business inside the corporate limits of the City of Port Angeles.

If a specific maturity date is required, either for cash flow purposes or for conformance to maturity guidelines, bids will be requested for instruments which meet the maturity requirement. If no specific maturity is required, a market trend analysis will determine which maturities would be most advantageous.

The City shall not knowingly make direct investments in companies supporting policies contrary to the U.S. Government position on Human Rights.

13. Internal Control

The controls shall be designed to prevent losses of public funds arising from fraud, employee error, misrepresentation of third parties, unanticipated changes in financial markets, or imprudent actions by employees and officers of the City.

Training should be provided to staff in investments, and personnel should keep current with financial development by participating in GFOA and MTA of US and Canada, subscribing to financial journals and periodicals, and participating in continuing education in investment management.

Controls deemed most important include: control of collusion, separating transaction authority from accounting and record keeping, custodial safekeeping, clear delegation of authority, specific limitations regarding securities losses and remedial action, written confirmation of telephone transactions, minimizing the number of authorized investment officials, documentation of transactions and strategies, and code of ethics standards. Appendix C shows the internal control strategy.

14. Performance Standards

The investment portfolio shall be designed to attain a market-average rate of return throughout budgetary and economic cycles, taking into account the City's investment risk constraints, the cash flow characteristics of the portfolio, and State and local laws and ordinances that restrict investments.

14.1 Market Yield

The basis used by the City Treasurer to determine whether market yields are being achieved shall be the 12-month moving average of the two-year Treasury.

15. Reporting

The City Treasurer is charged with the responsibility of preparing a report on investment activity.

15.1 Quarterly Reports

The City Treasurer shall submit a quarterly investment report to the City Council.

16. Distribution of Income

Interest income received shall be distributed monthly from the common portfolio to all participating funds in the following order:

16.1 Payment to Each Fund

Payment to each fund of an amount based on the ending cash balance included in the common portfolio for the earning period.

17. Investment Policy Adoption

The City of Port Angeles' investment policy shall be adopted by a resolution of the City Council. The policy shall be reviewed on an as-needed basis and any modifications made thereto must be approved by the City Council.

Responsibilities of the Treasurer Function

Functions	Responsibilities
1. Authorization of investment transactions <ul style="list-style-type: none"> • Formal investment policy <ul style="list-style-type: none"> - Prepared by - Adopted by 	Treasurer/Finance Director City Council
2. Execution of investment transactions	Treasurer/Finance Director
3. Timely recording investment transactions <ul style="list-style-type: none"> • Recording of investment transactions in Treasurer's records • Recording of investment transactions in the accounting records 	Treasurer Accounting Staff Accounting Staff
4. Verification of investment, i.e., match broker confirmation to Treasurer's records	Accounting Staff
5. Safeguarding of Assets and Records <ul style="list-style-type: none"> • Reconciliation of Treasurer's records to accounting records • Reconciliation of Treasurer's records to bank statement and safekeeping records • Review of <ul style="list-style-type: none"> a. Financial institution's financial condition b. Safety, liquidity, and yields of investments • Maintaining complete and current financial institution and brokerage company files • Periodic reviews of collateral 	Treasurer Accounting Staff Accounting Staff Finance Director Accounting Staff Finance Director
6. Management's periodic review of the investment portfolio in conformance to stated investment policy <ul style="list-style-type: none"> • Monthly • Quarterly 	Finance Director/ City Manager City Council
7. Annual review of the Investment Policy and Investment Program	Treasurer/Finance Director
8. Changes in the Investment Policy <ul style="list-style-type: none"> • Prepared by • Adopted by 	Treasurer/Finance Director City Council

Appendix D

Glossary

Glossary of Cash Management Terms

The following is a glossary of key investing terms, many of which appear in the City of Port Angeles 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 Life - 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.

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.

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.

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 the principal repayment, 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 \$100,000 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.

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 institutions. Security holder is protected by 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.

Market Risk - The risk that the value of a security will rise 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 establishes 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. Its 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. (Price Appreciation) + (Dividends paid) + (Capital Gains) = 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.