Council Meeting Date: April 28, 2003 **Agenda Item:** 9(a)

CITY COUNCIL AGENDA ITEM

CITY OF SHORELINE, WASHINGTON

AGENDA TITLE:	Adoption of Resolution Number 204, which adopts a revised Investment policy
DEPARTMENT:	Finance
PRESENTED BY:	Debbie Tarry, Finance Director AL Juarez, Financial Operations Manager

PROBLEM/ISSUE STATEMENT:

In July 1995 the City adopted Financial Policies that included policies related to the investment of City funds. Since that time the accounting profession has updated their recommended best practices applicable to the investment of public funds.

A resolution is attached that would adopt updated investment policies in order to establish a prudent investment program. This policy revision is intended to have City policies consistent with the model recommended by the Government Finance Officers Association (GFOA) and the Municipal Treasurers Association of the United States and Canada (MTA US &C). Additionally this policy revision is consistent with guidelines as presented by the WA State Auditors Office. Since the prudent investment of public funds is a key responsibility of government officials entrusted with public monies, recommended business practices include the adoption of formal investment policies that address investment objectives, define risk tolerance, assign responsibility, and establish control over the investment process. The updated investment policies will allow the City to develop an investment program to maximize its investment returns within the primary objectives of safety and liquidity.

FINANCIAL IMPACT:

This action has no monetary financial and/or budgetary implications. The implementation of the investment policies may result in increased investment earning.

RECOMMENDATION

Staff recommends that Council adopt Resolution No. 204, which repeals Section III of Resolution No. 37, adopted in 1995, and provides updated policies for control and accountability over the City's Investment program.

Approved By: City Manager ___ City Attorney

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INTRODUCTION

The prudent investment of public funds is a key responsibility of government officials entrusted with public monies. It is also one of the most visible aspects of public office as it is under intense public scrutiny. The success of an investment program can have far-reaching effects on the smooth functioning of the government and on the citizens it serves.

The City's investment program must conform to federal laws, state statutes, local ordinances, and internal policies and procedures. Internal controls should be in place to ensure that investment activities comply with all applicable statutes and policies.

Investment policies provide the framework for City staff to develop and implement an investment program that balances the need to maximize investment earnings with the necessity to make prudent investment choices.

BACKGROUND

Current Financial Policies, which address the City's investment program, were adopted via Resolution No. 37, dated July 31, 1995. These policies are outdated and no longer conform to "Recommended Practices for State and Local Governments."

DISCUSSION

Cash management has grown in importance to government entities of all sizes and is now considered a key element of a sound financial management program. While investing represents only one portion of a cash management program, it is a crucial component.

Besides legality, a government's foremost investment objective should be safety of principal. Governments are given money by the public to carry out the public's business. It is the government's fiduciary responsibility to keep that money intact to conduct its business.

Governments must maintain sufficient liquidity to meet operating requirements. Investments in long-term instruments may be considered if it is clearly demonstrated that these funds will not be required for immediate operating needs.

Governments depend on investment income to supplement other revenue therefore investment officials should be encouraged to earn the highest yields possible consistent with safety of principal and liquidity requirements.

Key differences that have been carefully presented in the proposed policy in comparison to the policy adopted in 1995, include:

- Clarification of policy scope
- Policy is applicable to all City funds
- Established performance standards
- States objectives (safety, liquidity, and return on investment)

- Explicit delegation of authority
- Definition of ethical behavior and conflicts of interest
- Definition of the City's investment strategy
- Defines the method of policy adoption

RECOMMENDATION

The City's policies are subject to continuous review and evaluation in order to assure a degree of accountability and efficiency that is worthy of the public trust. Staff recommends that Council adopt Resolution No. 204, which repeals Section III of Resolution No. 37, adopted in 1995 and provides updated guidelines for control and accountability over the City's Investment program.

ATTACHMENTS

Attachment A - Resolution Number 204
Attachment B – Recommended Investment Policies
Attachment C – Investment Policies adopted in 1995

ATTACHMENT A

RESOLUTION NO. 204

A RESOLUTION OF THE CITY OF SHORELINE, WASHINGTON REVISING FINANCIAL POLICIES REGARDING THE INVESTMENT OF PUBLIC FUNDS

WHEREAS, the City Council wishes to provide excellent financial management of the City's investment program; and

WHEREAS, the City's current investment policies, adopted in 1995, do not reflect the Government Finance Officers Association (GFOA) recommended best practices applicable to an investment program; and

WHEREAS, the City Council wishes to set out guidelines for the City Manager in the administration of a City investment program; and

WHEREAS, a comprehensive financial policy provides a solid foundation to meet the City's needs; and

WHEREAS, the City Council wishes to revise the Financial Policies associated with the investment of Public Funds; NOW, THEREFORE,

BE IT RESOLVED BY THE CITY COUNCIL OF THE CITY OF SHORELINE, WASHINGTON, AS FOLLOWS:

Section 1. The City Council hereby repeals section III of the Financial Management Policies (Resolution No. 37, dated July 31, 1995).

Section 2. The City Council hereby authorizes the Finance Department to implement administrative policy and procedures required to protect and account for City Investments.

Section 3. The City Council hereby adopts Investment Policies to be followed

the City's Cash Management Program (Attachment B).

ADOPTED BY THE CITY COUNCIL ON APRIL 28, 2003.

_____
Scott Jepsen, Mayor

ATTEST:

_____
Sharon Mattioli, CMC
City Clerk

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ATTACHMENT B

City of Shoreline
Investment Policy

1.0 Policy:
It is the policy of the City of Shoreline to invest public funds in a manner, which will provide the highest investment return with the maximum security while meeting it's daily cash flow demands. All investments shall conform to all Washington statutes governing the investment of public funds.

2.0 Scope:
It is intended that these policies apply to investment activities of all reserves and inactive cash under the direct authority of the City of Shoreline.

2.1 Pooled Investments:
Investments for the City will be made on a pooled basis and include the financial assets of all funds of the City. These funds, presented in the City's Annual Financial Report, include:

2.1.1 The General Fund (001)

2.1.2 Special Revenue Funds (100 series of fund numbers), to account for the proceeds of specific revenue sources (other than expendable trusts, or for major capital projects) that are legally restricted to expenditure for specified purposes.

2.1.3 Capital Project Funds (300 series of fund numbers) to account for financial resources to be used for the acquisition or construction of major capital facilities and infrastructure (other than those financed by proprietary funds and trust funds) that include the construction project funds.

2.1.4 Internal Service Funds (500 series of fund numbers), to account for the financing of goods or services provided by one department or agency to other departments or agencies of the governmental unit, or to other governmental units, on a cost reimbursement basis, represented by the Equipment Replacement, Equipment Rental, and Unemployment reserve Funds.

2.1.5 Any new fund created by the Council unless specifically exempted by the Council.

3.0 Prudence:
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.

3.1 The standard of prudence to be used by investment officials should be the "prudent person," standard and shall be applied in the context of managing an overall portfolio. Investment officers acting in accordance with written procedures, 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.

4.0 Objective:
The primary objectives in priority order of the City's investment activity shall be safety, liquidity, and return on investment.

4.1 Safety: Safety of principal is the foremost objective of the City of Shoreline. Investments of the City shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. To obtain this objective, diversification is required so that potential losses on an individual security do not exceed the income generated from the remainder of the portfolio.

4.2 Liquidity: The City's investment portfolio will remain sufficiently liquid to enable the City to meet all operating requirements, which may be reasonably anticipated.

4.3 Return on Investment: The City's investment portfolio shall be designed with the objective of obtaining a market rate of return throughout budgetary and economic cycles, taking into account the City's investment risk constraints, the City's investment objectives, and the cash flow characteristics of the portfolio.

5.0 Delegation of Authority:
By the adoption of this policy, the management of inactive cash and the investment of funds identified in paragraph 2.1 are the responsibility of the City Manager or his/her designee as identified within the City of Shoreline Municipal Code. Management responsibility for the investment program is hereby delegated to the Finance Director or his/her designee, who shall establish written procedures for the operation of the investment program consistent with this investment policy.

In the execution of this delegated authority, the Finance Director or his/her designee may establish accounts with qualified financial institutions and broker/dealers for the purpose of effecting investment transactions in accordance with this policy. The criteria used to select qualified financial institutions and broker/dealers are identified in paragraph 7.0 of this policy.

5.1 Investment Procedures: The procedures should include reference to safekeeping, master repurchase agreements, wire transfer agreements, custody agreements and 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 and the procedures established by the Finance Director or his/her designee.

6.0 Ethics and Conflicts of Interest:
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 Finance Director or his/her designee any material financial interest 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 the City's portfolio. Employees and officers shall subordinate their personal investment transactions to those of the City of Shoreline, particularly with regard to the timing of purchases and sales.

7.0 Authorized Financial Dealers and Institutions:
The Finance Director or his/her designee will maintain a list of financial institutions authorized to provide investment services. In addition, a list will also be maintained of approved Security Brokers/Dealers selected by credit worthiness and who are authorized to conduct business in the State of Washington. No public deposit may be made except in a qualified depository in the State of Washington as provided in Chapter 39.58 RCW. All brokers/dealers and financial institutions who desire to do business with the City must supply the Finance Director with annual audited financial statements, proof of National Association of Securities Dealers certification, and certification of having read the City's investment policy. The Finance Director will periodically conduct an annual review of the financial condition of all financial institutions and broker /dealers with whom the City invests ensuring that a current audited financial statement and other supplementary information required by the City is current.

8.0 Authorized and Suitable Investments:
The City of Shoreline is empowered to invest in any of the securities as defined by RCW 35A.40.050 "Fiscal - Investment of Funds." In general, these include:

8.1 Investment deposits, including certificates of deposit, with qualified depositories defined in Chapter 39.58, RCW.

8.2 Certificate notes or bonds of the United States, or other obligations of the United States, or its agencies, or any corporation 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 Loans, Bank notes and bonds, Federal Farm Credit Bank consolidation notes and bonds, Federal National Mortgage Association Notes, and guaranteed certificates of participation.

8.4 Bankers acceptances purchased on the secondary market.

8.5 Repurchase agreements for securities listed in 2, 3 and 4 above, provided that the transaction is structured so that the City of Shoreline obtains control over the underlying securities, and a master repurchase agreement has been signed with the bank or dealer.

8.6 Washington State Local Government Investment Pool.

9.0 Investment Strategy:

9.1 Pooled Investments. A buy and hold strategy will generally be followed; that is, investments once made will usually be held until maturity. A buy and hold strategy will result in unrealized gains or losses as market interest rates fall or rise from the coupon date of the investment. Unrealized gains or losses, however, will diminish as the maturity dates of the investments are approached or as market interest rates move closer to the coupon rate of the investment. A buy and hold strategy requires that the portfolio be kept sufficiently liquid to preclude the undesired sale of investments prior to maturity. Occasionally, the Finance Director or his/her designee may find it advantageous to sell an investment prior to maturity, but this should only be on an exception basis and only when it is clearly favorable to do so.

9.2 Investments held separately. Investments held separately for bond proceeds will follow the trust indenture for each issue.

10.0 Collateralization:

Investments in time certificates of deposit shall be fully insured up to $100,000 by the Federal Deposit Insurance Corporation (FDIC) or the Federal Savings & Loan Insurance Corporation (FSLIC), as appropriate. Additionally the Public Deposit Protection Commission (PDPC) provides security by protecting public deposits, which exceed the amount insured by the FDIC. The PDPC also minimizes participating depositaries liability for defaulting institutions

In order to provide a level of security for all funds, collateralization will be required on certificates of deposit and repurchase agreements pursuant to RCW 39.58.050 and 39.59.020. Repurchase Agreements shall be collateralized at 102% of par value plus accrued interest. Only Securities authorized to be purchased by the City will be accepted as collateral and said instruments will always be held by an independent third party with which the City has a current custodial agreement. The independent third party shall provide a clearly marked evidence of ownership (safekeeping receipt) for the City's records.

The right to make substitutions of an equal or greater amount of such collateral at any time is granted.

11.0 Safekeeping and Custody:

All security transactions, including collateral for repurchase agreements entered into by the City of Shoreline, shall be conducted on a delivery versus payment basis. Securities

purchased by the City will be delivered against payment and held in a custodial safekeeping account. A third party custodian designated by the Finance Director or his/her designee will hold securities and safekeeping receipts will evidence all transactions.

12.0 Diversification:
In order to reduce overall portfolio risk while attaining a benchmark average rate of return, the City will diversify its investments by security type, issuing institution, and terms of maturity. The diversification concept in a cash management fund thus will include prohibition against over concentration in a specific maturity sector as well as restricting the reliance on specific risk instruments and issuers. With the exception of U.S. Treasury Securities and the WA State Local Government Investment Pool no more than fifty percent (50%) of the City's total investment portfolio will be invested in a single security type, with a single financial institution or scheduled for maturity in a single date sector.

13.0 Maximum Maturities:
To the extent possible, the City will attempt to match its investments with anticipated cash flow requirements. Unless matched with a specific cash flow, the City will not directly invest operating funds in securities maturing in more than two years from the date of purchase. However, the City may collateralize repurchase agreements using longer dated investments.

Reserve or construction in progress funds may be invested in securities maturing up to five years after the purchase date if such investments are made to coincide as nearly as practical with the expected use of the funds

14.0 Internal Controls:
The development of internal controls is the responsibility of the City's management. Authority to establish and maintain internal controls is by this policy assigned to the Finance Director or his/her designee. Either an independent auditor or an independent committee, as determined appropriate by the Finance Director or his/her designee shall conduct periodic reviews of said internal controls in order to assure compliance with investment policy, procedure and State statute. Periodic reviews may result in recommendations to revise or change procedures in order to improve effectiveness and/or efficiency.

15.0 Performance Standards:
The City of Shoreline investment portfolio will be designed to obtain a market average rate of return in budgetary and economic cycles, taking into account the City's investment risk constraints, investment objectives and cash flow needs.

15.1 Market Yield. The City's investment strategy is passive and yield objectives are just as important as internal controls. Given this strategy, the basis used to determine whether the market yields are being achieved shall be to identify a comparable benchmark to our portfolio investment duration. This benchmark shall be periodically reviewed for effectiveness and applicability. The present benchmark has been identified as the annual average of the Washington State

Local Government Investment Pool (LGIP). Average rate data will be derived from the Office of the State Treasurer, custodian and administrator of the LGIP.

16.0 Reporting:
Periodic investment reports to policymakers and elected officials provide necessary written communication regarding investment performance, risk analysis and adherence to policy provisions. Given this theory, investment reports shall be incorporated within routinely scheduled quarterly financial reports submitted to management and Council that provide a clear picture of the status of the current investment portfolio. The investment report should include, at a minimum: (a) a listing of individual securities held at the end of the reporting period by authorized investment category, (b) life and final maturity date of all investments listed, (c) earnings rate, (d) par value, and (e) percentage of the portfolio represented by each investment category.

17.0 Adoption of Policy:
The City of Shoreline investment policy shall be adopted by resolution of the City Council. The policy is subject to continuous review and evaluation primarily by the Finance Director and his/her designee in order to assure a degree of accountability and professionalism that is worthy of the public trust. All recommended modifications must be approved and adopted by resolution of the City Council.

GLOSSARY

Agencies. Federal Agency Securities, the price at which the securities are offered.

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

Bid. The price offered by a buyer of securities. (When you are selling securities, you ask for a bid.) See Offer.

Broker. A broker brings buyers and sellers together for a commission.

Certificate of Deposit (CD). A time deposit with a specific maturity evidenced by a certificate. Large denominations CD's 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.

Commission. The price offered for securities 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 have a position in the money market. Brokers are active in markets, in which banks buy and sell money and enter dealer markets.

Coupon. An annual rate of interest that a bond issuer promises to pay the bondholder on the balance of the face value.

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

Debenture. A bond secured only by the general credit of the issuer.

Delivery versus Payment. There are two methods of delivery of securities: delivery versus payment and delivery versus receipt (also called free). Delivery versus payment is delivery of securities with an exchange of money for the securities. Delivery versus receipt is delivery of securities with an exchange of a signed receipt for the securities.

Discount. The difference between the cost price of a security and its value at maturity when quoted at lower than face value. A security selling below original offering price shortly after sale also is considered to be 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. Dividing investment funds among a variety of securities offering independent returns.

Duration. The measurement of sensitivity of a security's market value or price. It s the average time until receipt of the weighted present value of the cash flows, expressed in years.

Factor. The decimal number representing the proportion of the outstanding principal balance of a security to it's original certificate amount currently remaining.

Federal Credit Agencies. Agencies of the Federal government set up to supply credit to various classes of institutions and individuals, e.g., S&L's, 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 Rate. The rate of interest at which Federal funds are traded. This rate is currently pegged by the Federal Reserve through open market operations.

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). 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 & Urban Development, HUD. It is the largest single provider of residential mortgage funds in the 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.

Float. The amount of money represented by checks outstanding and in the process of collection.

Freddie Mac. The Federal Home Loan Mortgage Corporation (FHLMC) was created in July 1970 to promote development of a nation-wide secondary market in conventional residential mortgages. The FHLMC buys residential mortgages and then resells them via the sale of mortgage related instruments. The FHLMC may purchase mortgages only from financial institutions that have their deposits or accounts insured by agencies of the federal government.

Full Faith and Credit. A pledge of the general taxing power of a government to repay debt obligations (typically used in reference to bonds).

Government National Mortgage Association (GNMA OR GINNIE MAE). The 1968 partition of the Federal National Mortgage Association spawned the Government National Mortgage Association. Ginnie Mae is a wholly government-owned corporation within the Department of Housing and Urban Development. Ginnie Mae's mission is to make real estate investment more attractive to institutional investors which it has done by designing and issuing, partly in conjunction with private financial institutions, mortgage-backed securities for which an active secondary market has developed. These securities are referred to as pass-through securities because payment of interest and principal on mortgages is passed on to the certificate holders after deduction of fees for servicing and guarantee. These securities carry Ginnie Mae's guarantee of timely payment of both principal and interest and are backed by the full faith and credit of the U.S. Government.

Internal Control. A plan of organization for purchasing, accounting, and other financial activities which, among other things, provides that:

- The duties of employees are subdivided so that no single employee handles a financial action from beginning to end.
- Proper authorization from specific responsible officials are obtained before key steps in the processing of a transaction are completed; and
- Records and procedures are arranged appropriately to facilitate effective control.

Investment. Securities and real estate purchased and held for the production of income in the form of interest, dividends, rentals or base payments.

Investment Instrument. The specific type of security, which a government purchases, and holds.

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 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.

Offer. The price asked by a seller of securities. (When you are buying securities, you ask for an offer.) See Bid.

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.

Performance Measures. Specific quantitative measures of work performed within an activity or program (e.g., total interest earned). Also, a specific quantitative measure of results obtained through a program or activity (e.g., comparison of portfolio yield to six-month Treasury bill).

Premium. The amount by which a security is selling above par.

Portfolio. A collection of securities held by an investor.

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 insight. Primary dealers include Securities and Exchange Commission (SEC) registered securities broker-dealers, banks, and a few unregulated firms.

Prudent Person Rule. An investment standard. Washington law requires that a fiduciary or trustee may invest money only in a list of eligible investments pursuant to the text of RCW 39.59.020; 35.39.030; 43.84.080; and 43.250.040. In some other states the trustee may invest in a security if it is one which would be bought by a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital.

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.

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. 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 security deposits of public monies.

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

Structured Notes. Notes issued by Government Sponsored Enterprises (Federal Home Loan Bank, Federal National Mortgage Association, Student Loan Marketing Association, etc) and Corporations which have imbedded options (e.g., call features, step-up coupons, floating rate coupons, derivative based returns) into their debt structure. Their market performance is impacted by the fluctuation of interest rates, the volatility of the imbedded options and shifts in the shape of the yield curve.

Tax Anticipation Notes. Notes issued in anticipation of taxes which are retired usually from taxes collected.

Treasury Bills. A non-interest bearing discount security issued by the U. S. Treasury to finance the national debt. Most bills are issued to mature in three months, six months or one year.

Treasury Bond. Long-term U. S. treasury securities having initial maturities of more than ten years.

Treasury Notes. Intermediate term coupon bearing U. S. Treasury securities having initial maturities of from one to ten years.

Uniform Net Capital Rule. Securities and Exchange Commission requirement that member firms as well as nonmember broker-dealers in securities maintain a maximum ratio of indebtedness to liquid capital of 15 to 1; also called 'net capital rule' and 'net capital ratio'. Indebtedness covers all money owed to a firm, including margin loans and commitments to purchase securities, one-reason new public issues are spread among members of underwriting syndicates. Liquid capital includes cash and assets easily converted into cash.

Weighted Average Life. The weighted average number of years from the security's issuance until each principal dollar is returned to the investor.

Yield. The rate of annual income return on an investment, expressed as a percentage.

- INCOME YIELD is obtained by dividing the current dollar income by the current market price for the security.
- NET YIELD or YIELD TO MATURITY is the current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond.

ATTACHMENT C

III. INVESTMENTS

The City's policy applies to the investment of all City funds, with the exception of pension funds or money set aside in a trust account for special purposes, such as a refunding trustee, or financial requirements of Federal, State or local law which would prohibit the implementation of this policy.

A. Types of Investments

The City may invest in any of the securities identified as eligible investments as defined by RCW 35A.40.050 "Fiscal - Investment of Funds." In general, these consist of:

1. Investment deposits (Certificates of Deposit) with qualified public depositories as defined in Chapter 39.58 RCW.

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 whose securities carry full faith and credit guarantees.

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, Federal National Mortgage Association and Federal Intermediate Credit Bonds, notes, debentures, and guaranteed certificates of participation.)

4. Bankers' acceptances purchased on the secondary market.

5. Repurchase agreements for securities listed in two, three, and four above, provided the transaction is structured so the City obtains ownership and control over the underlying securities.

6. Certificates, notes, and bonds of the State of Washington or political subdivisions, including L.I.D. warrants, notes, or bonds of the Cities of Washington.

Investment authority of special funds such as the Firemen's Pension Fund may vary from the above based on applicable laws.

B. Maturities

The investment program is intended to provide adequate liquidity to meet cash flow requirements.

ATTACHMENT C

The minimum requirement for liquidity of operating funds when taken as a whole is 25% of the estimated annual operating budget revenues which shall consist of the following:

- Cash balances;
- Fixed maturities due within 30 days;
- State of Washington Local Government Investment Pool;
- Open repurchase agreements;
- Market value of marketable securities, including accrued interest. No more than 60% of the minimum requirement may be in this category and Interfund Loans;
- Loans to other funds which could be remarketed to the private sector within 30 days. No more than 30% of the minimum requirement may be in this category.

Operating funds (unless pooled) may be invested in maturities not to exceed 18 months unless the Director of Administrative Services has agreed to the longer maturity. Pooled investments may occur in the intermediate market, those investments maturing between 2 and 10 years.

Non-operating funds may be invested in maturities not to exceed 10 years unless the Director of Administrative Services has agreed to a longer maturity and reported same to the Budget and Finance Committee of the City Council. These funds include, but are not limited to:

- Cumulative Reserve Funds
- Debt Service Reserves
- Pension Funds
- Endowment Funds

C. Risk

Speculative investments are not allowed. The City will not purchase investments which at the time of investment are not intended to be held to maturity within the maturity guidelines mentioned above.

D. Selection of Banks and Dealers

The City of Shoreline shall seek to conduct its investment transactions with several competing, reputable investment securities dealers and brokers. Staff shall establish procedures for the competitive purchasing and selling of securities.

While not an absolute restriction, dealers should normally be chosen from the western Washington area.

1. Selection of a Primary Bank

The selection of a primary bank for general banking services will be accomplished through a formal competitive bidding process. Among the services required of a primary bank is the availability of safekeeping services, which must include the ability to transfer daily by federal wire, and investment securities to and from other financial institutions. The safekeeping services must also offer a "delivery vs. payment" option.

2. Selection of Bank and Thrift Institutions

Institutions used by the City of Shoreline must appear on the Approved Depository List required by State law to be designated by the City Council, which must also be approved by the Washington State Public Depository Protection Commission (PDPC) as eligible for the deposit of public funds.

3. Selection of Brokers/Dealers (Including Bank Investment Departments)

The City may deal with all securities dealers classified as reporting dealers affiliated with the New York Federal Reserve Bank as primary dealers, and with those falling under the supervision of Federal Bank Examiners, without further certification.

Other Securities Dealers may be certified by the Finance Manager to conduct business with the City. As part of the certification process, the Finance Manager will obtain a written representation from an officer or Senior Management Representative of each dealer which describes or provides a profile of existing clients, securities specialties, the breadth of the market covered, research capabilities, an experience profile of senior and Shoreline assigned staff, licenses held, adherence to appropriate regulatory standards, size and capitalization. The latter shall be verified by certified audited financial statements.

The Finance Manager will prepare a procedure which describes the selection criteria for dealers and a process for maintaining current dealer information in a file.

Broker dealers doing business with the City will be provided a copy of this investment policy and will be expected to assure the transactions accomplished for the City fall within these policy boundaries.

E. Bidding of Investments

Investments shall be placed through an informal bidding process. Generally, bids should be taken from several institutions. Although the City desires to award bids to the highest bidder, subjective judgment may be required in awarding the bid for such things as size of the investment, cost of placing the investment, time available to place the investment (overhead), Prudent Person Standard, and the general guidelines of this policy.

F. Diversification

By investing in several different instruments with different issuers, failure of a particular transaction to occur as planned is not likely to cause a major cash flow crisis. Our policy is to assure no single institution or security is invested into such an extent that a delay of liquidation at maturity is likely to cause a current cash flow emergency.

G. Administration

The Finance Manager has the operational responsibilities of the investment program, and shall establish a system of controls to regulate these delegated activities and responsibilities. Employees responsible for investments shall be bonded through the City Risk Management Policy.

H. Collateral. Safekeeping and Custody

All safekeeping investments shall be accomplished on a "delivery vs. payment" basis (DVP). (This means the instrument being purchased is delivered to us or our designated agent before payment is released.)

In the case of Certificates of Deposit, the certificates are delivered to and held by the Finance Manager's office.

The market value of securities used in repo transactions must be at least equal to the amount invested and every effort must be made to maintain value to at least the amount invested. Repo's without a margin for market fluctuation must be subject to immediate cancellation prior to the agreed term or require additional collateral to assure adequate market value coverage.

In addition to the custody of securities, concern must also be shown for the quality of securities expressed in terms of their reliability or likelihood of being redeemed at full value at maturity and of making interest payments on schedule.

I. Booking of Losses on Sale of Investment

No loss will be deemed to have occurred on the prematurity exchange of one security for another unless the proceeds of the sale, plus interest earned on the original and subsequent investment, calculated to the original maturity date, is less than the gross proceeds of the original investment at maturity. Loss by default of an issuer will be determined by subtracting any amount received from the collateral or other security devices, from the original investment cost plus interest, calculated to the date of recovery.

J. Written Investment Procedures

The Finance Manager shall provide and maintain written investment procedures consistent with this policy. These procedures shall be approved by the City Administrative Services Director.

K. Reporting· Requirements

The Finance Manager shall provide monthly reports to the Administrative Services Director. The report will contain a summary of investment position, yields, maturities, and other such information which may be required by report users.

L. Prudent Person Standard

Investments shall be made with judgment and care under prevailing circumstances, which persons of prudence, discretion and intelligence would use in the management of their own affairs, not for speculation, but for investment purposes (Prudent Person Standard).

The standard of prudence to be used by investment officials shall be the "prudent person" and shall be applied in the context of managing an overall portfolio. Investment officers meeting the "prudent person" standard shall be relieved of personal responsibility for an individual security's subsequent performance, provided appropriate action is taken to control adverse developments.

Investment officials shall recognize the investment portfolio is subject to public review and evaluation. The overall program shall be designed and managed with a degree of professionalism which is worthy of the public trust. The governing body recognizes that in a diversified portfolio, occasional measured losses are inevitable and must be considered within the context of the overall portfolio's investment return -- provided adequate diversification has been implemented.