Council Action Summary – April 9, 2019

Agenda Location: Consent Resolution

G) Resolution: Approve Update to the City's Investment Policy

Attachments:

- Resolution
- City's Investment Policy

Summary: The purpose of the City's Investment Policy is to formalize the framework for the City of Rolling Meadows' investment activities. The City's Investment Policy has not been updated for some time. This update is to include language to be in compliance with municipal securities rules as well as applicable state and federal statutes that were recently approved.

The City Rolling Meadows invests public funds in a manner which will provide the highest investment return with the maximum security while meeting the daily cash flow demands and liquidity needs of the City.

On an annual basis, this Policy is reviewed by the City Attorney and the City's independent audit firm who are licensed certified professional accountants (CPAs).

Previous Council Action:

- City Council approval of previous Investment Policy.

Staff Recommendation:

Accept the update to the City's Investment Policy.

Resolution No. 19-R-53

A RESOLUTION APPROVING AN UPDATE TO THE CITY'S INVESTMENT POLICY

WHEREAS, the purpose of the City's Investment Policy is to formalize the framework for the City of Rolling Meadows' investment activities. This Policy applies to all of the City's financial assets and is intended to be broad enough to allow the City to function properly within the parameters of responsibility and authority, while adequately safeguarding such assets.

WHEREAS, all transactions involving the City's financial assets and related activity, shall be administered and conducted in accordance with this Policy.

WHEREAS, on an annual basis, this Policy is reviewed by the City Attorney, Staff and the City's independent audit firm who are licensed certified professional accountants (CPAs).

WHEREAS, the investment program shall be operated in conformance with governing legislation and other legal requirements.

NOW THEREFORE, be it resolved by the City Council of the City of Rolling Meadows, that the City Council approves the update to the City's Investment Policy.

Yeas:

Nays:

Absent:

Passed and approved this 9th day of April, 2019.

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Len Prejna, Mayor

ATTEST:

____
Judith Brose, Deputy City Clerk

City of Rolling Meadows
Investment Policy
April 2019

City of Rolling Meadows
Investment Policy

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I. Investment Policy Purpose

The purpose of this Investment Policy (Policy) is to formalize the framework for the City of Rolling Meadows' investment activities. The City of Rolling Meadows, as a municipality, has a fiduciary responsibility to properly account and manage public funds. This Policy applies to all of the City's financial assets and is intended to be broad enough to allow the City to function properly within the parameters of responsibility and authority, while adequately safeguarding such assets. All transactions involving the City's financial assets and related activity, shall be administered and conducted in accordance with this Policy.

The City Rolling Meadows invests public funds in a manner which will provide the highest investment return with the maximum security while meeting the daily cash flow demands of the City.

On an annual basis, this Policy is reviewed by the City Attorney, Staff and the City's independent audit firm who are licensed certified professional accountants (CPAs).

II. Governing Authority

Legality
The investment program shall be operated in conformance with governing legislation and other legal requirements.

III. Responsibility

1. City Council: The City Council will retain ultimate fiduciary responsibility for the City's deposits and investments. The City Council will receive at least quarterly reports on the City's deposits and investments.

2. Investment Officer: Authority to manage the investment program is granted to the Finance Director as designated by 30 ILCS 235/2.5(a)(7). Management responsibility for the operation of the investment program is hereby designated to the Finance Director, with the advice and consent of the City Manager, who shall act in accordance with established written procedures and internal controls for the operation of the investment program consistent with this Policy.

IV. Scope

This Policy applies to the investment of all funds, excluding the investment of employees' retirement funds [Police Pension Fund, Fire Pension Fund, and the Illinois Municipal Retirement Fund (IMRF).] (The employees' retirement funds each has a separate investment policy that is administered by each of the pension funds separately.) The City's Investment Policy applies to the investment activities of the City's Fund including to all cash of the General Fund, Special Revenue Funds, Capital Project Funds, Debt Service Funds, Trust and Agency Funds, and any other Funds that may be created from time-to-time, shall be administered with the provisions of this Policy.

1. *Pooling of Funds*
Except for cash in certain restricted and special funds, the City will consolidate cash and reserve balances from all funds to maximize investment earnings and to increase efficiencies with regard to investment pricing, safekeeping and administration. Per SEC

Rule 15B (Municipal Advisor Rule), the Policy states that the pooled/invested funds exclude municipal bond proceeds. Bond proceeds are invested per this Policy with PMA Investments and are separately accounted for to the City of Rolling Meadows. The City Council will receive at least quarterly reports on the investment of the City's bond proceeds.

Investment income will be allocated to the various funds based on their respective participation and in accordance with generally accepted accounting principles.

V. Investment Policy Objectives

The primary objectives of investment activities, in order of priority, shall be safety, liquidity, and return:

1. Safety

Safety of principal is the foremost objective of the investment program. 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. <u>Credit Risk</u>

The City will minimize credit risk, which is the risk of loss of all or part of the investment due to the failure of the security issuer or backer, by:

- Limiting investments to the safest types of securities as outlined in this Policy.
- Pre-qualifying and conducting ongoing due diligence of the financial institutions, broker/dealers, intermediaries, and advisers with which the City will do business in accordance with this Policy.
- Diversifying the investment portfolio so that the impact of potential losses from any one type of security or from any one individual issuer will be minimized.

b. <u>Interest Rate Risk</u>

The City will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by:

- Structuring the investment portfolio so that security maturities match 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 and limiting individual security maturity as well as the average maturity of the portfolio in accordance with this Policy.

2. Liquidity

The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may 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). Alternatively, a portion of the portfolio may be placed in money market mutual funds or local government investment pools which offer same-day liquidity for short-term funds.

3. Return

The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core investments are limited to relatively low risk securities in anticipation of earning a fair 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 loss of principal;
- Selling a security and reinvesting the proceeds that would improve the quality, yield, or target duration in the portfolio may be undertaken;
- Unanticipated liquidity needs of the portfolio require that the security be sold.

VI. Standards of Care

1. *Prudence*

The standard of prudence to be used by the investment official shall be the "prudent person" standard and shall be applied in the context of managing an overall portfolio. The Finance Director and designees acting in accordance with written procedures and this 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 the liquidity and the sale of securities are carried out in accordance with the terms of this Policy.

2. *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 and management of the investment program, or that could impair their ability to make impartial decisions. Employees and investment officials shall disclose any material interests in financial institutions with which they conduct business, in accordance with applicable laws. They shall further disclose any personal financial/investment positions that could be related to the performance of the investment portfolio. Employees and officers shall refrain from undertaking personal investment transactions with the same individual with whom business is conducted on behalf of the City of Rolling Meadows.

3. *Delegation of Authority*

The management responsibility for the investment program of the City is hereby delegated to the Finance Director, who shall establish written procedures and internal controls for the operation of the investment program consistent with this Policy. 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. The Finance Director shall be responsible for all transactions undertaken and shall establish a system of internal controls to regulate the activities of subordinate officials.

- Performance of the portfolio shall be reported in the City’s Comprehensive Annual Financial Report (CAFR) and shall include portfolio composition and performance information.
- Material deviations from projected investment strategies shall be reported immediately to the City Manager.

VII. Authorized Financial Institutions

The Finance Director will maintain a lists of financial institutions authorized to provide depository and investment services. In addition, a list will be maintained of approved security broker/dealers selected by credit worthiness. These may include “primary” dealers or regional dealers that qualify under Security Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule). No public deposit shall be made except at a qualified public depository as established by state statutes.

All financial institutions and broker/dealers who desire to become qualified for investment transactions must supply to the City the following items:

- Audited financial statements demonstrating compliance with state and federal capacity guidelines.
- Proof of National Association of Security Dealers (NASD) certification (not applicable to Certificate of Deposit counterparties).
- Proof of state registration.
- Completed broker/dealer questionnaire.
- Evidence of adequate insurance coverage.
- Certification of having read and understood the City’s Investment Policy.

VIII. Safekeeping and Custody

1. *Delivery vs. Payment*
All trades of marketable securities will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible custody account prior to the release of funds.

2. Safekeeping
Securities will be held by an independent third-party custodian selected by the City as with all securities held in the City’s name. The safekeeping institution shall annually provide a copy of their most recent report on internal controls (Statement of Auditing Standards No. 70, or SAS 70).

3. *Internal Controls*
The Finance Director shall establish a system of internal controls, which shall be documented in writing. The internal controls shall be reviewed annually by Finance Director and the City’s Auditors. The controls shall be designed to prevent the loss of public funds arising from fraud, employee error, mis-representation by third parties, unanticipated changes in financial markets, or imprudent actions by employees and officers of the City of Rolling Meadows.

The internal controls structure shall address the following items:

- Control of collusion
- Separate 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.
- Dual authentication of wire transfers.
- Development of a wire transfer agreement with banks and third party-custodians.

IX. Suitable and Authorized Investments

The City of Rolling Meadows may invest in any type of security allowed for in Illinois Compiled Statutes (30 ILCS 235/2) regarding the investment of public funds. Approved investments include:

- U.S. government obligations, U.S. government agency obligations, which have a liquid market with readily determinable market values;
- Investment-grade obligations of state and local governments and public authorities;
- Interest bearing-savings accounts, interest-bearing certificates of deposit or interest-bearing time deposits or any other investments constituting direct obligations of any bank as defined by the Illinois Banking Act; and its insured by the Federal Deposit Insurance Corporation (FDIC);
- Short-term obligations of corporations organized in the United States with assets exceeding $500,000,0000 if (i) such obligations are rated at the time of purchase at one of the highest classifications established by at least two standard rating services and which mature not later than 180 days from the date of purchase, (ii) such purchases do not exceed 10% of the corporation's outstanding obligations and (iii) no more than 25% of the City's funds are invested in short-term obligations of corporations;
- Money market mutual funds registered under the Investment Company Act of 1940, provided that the portfolio of any such money market fund is limited to (1) bonds, notes, certificates of indebtedness, treasury bills or other securities now or hereafter issued, which are guaranteed by the full faith and credit of the United States of America as to principal and interest, (2) bonds, notes debentures, or other similar obligations of the United States of America, or its agencies, and its instrumentalities, or (3) agreements to repurchase such obligations.
- A Public Treasurers' Investment Pool created under the State Treasurer Act (Illinois Funds);
- Illinois Trust (formerly Illinois Institutional Investors Trust), IIIT Class;
- Illinois Metropolitan Investment Fund (IMET);
- Any other investment permitted by Illinois State Statute.

1. *Collateralization*
It is the policy of the City of Rolling Meadows in accordance with the Government Finance Officers Association's (GFOA) Recommended Best Practices on Collateralization of Public Deposits to require that funds on deposit in excess of FDIC limits be secured by collateral, including letters of credit (http://www.gfoa.org/best-practices). The City may accept the following as collateral:

  - U.S Government Securities
  - Obligations of Federal Agencies
  - Obligations of Federal Instrumentalities
  - Obligations of the State of Illinois
  - Obligations of the City of Rolling Meadows
  - General Obligation Bonds of other municipalities rated "AA" or better
  - Any other collateral identified in Illinois Compiled Statutes as acceptable for use by the Treasurer of the State of Illinois.

(The City reserves the right to accept/reject any form of the above named securities.)

The amount of collateral will note be less than 110% of the fair market value of the net amount of public funds secured. The ratio of fair market value of collateral to the amount of funds secured will be reviewed monthly and more frequently when the ratio declines below the level required.

Pledged collateral will be held in a safekeeping account and evidenced by a safekeeping agreement with monthly statements. The City's Auditors review the monthly statements during their Audit process. Collateral agreements will preclude the release of pledged assets without an authorized signature from the City of Rolling Meadows. Exchange of collateral of like value will be permitted by the City. To achieve savings for the City in lieu of collateralization, the City is eligible to use a letter of credit as a binding document that guarantees the payment of an obligation and is payable on demand. These options are reviewed on an annual basis.

2. *Repurchase Agreements*
Repurchase agreements shall be consistent with GFOA Recommended Practices on Repurchase Agreements (http://www.gfoa.org/best-practices).

X. Investment Parameters

1. *Diversification*
It is the Policy of the City to diversify its investment portfolios. To eliminate risk of loss resulting from the overconcentration of assets in a specific maturity, issuer, or class of securities, all cash and cash equivalent assets in all City funds shall be diversified by maturity, issuer, and security type. Diversification strategies shall be determined and revised periodically by the Finance Director for all funds except for the employees' retirement funds which are invested in separately from the City.

In establishing specific diversification strategies, the following general policies and constraints shall apply: Portfolio maturities shall be staggered to avoid undue concentration of assets in a specific maturity sector. Maturities selected shall provide for stability of income and reasonable liquidity.

No financial institution shall have on deposit more than 50% of the City's investment portfolio at one time, exclusive of U.S. Treasury securities held in safekeeping.

Commercial paper shall not exceed 25% of the City's investment portfolio at the time of placement.

- Liquidity shall be assured through practices ensuring that the next disbursement date and payroll date are covered through maturing investments or marketable U.S. Treasury bills.
- Positions in securities having potential default risk (e.g., commercial paper) shall be limited in size so that in case of default, the portfolio's annual investment income will exceed a loss on a single issuer's securities.
- Risks of market price volatility shall be controlled through maturity diversification and duration management.
- The Finance Director shall establish strategies and guidelines for the percentage of the total portfolio that may be invested in securities other than repurchase agreements, Treasury bills or collateralized certificates of deposit.

2. *Maximum Maturities*
To the extent possible, the City shall attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the City will not directly invest in securities maturing more than three (3) years from the date of purchase or in accordance with governing legislation. The City shall adopt weighted average maturity limitations consistent with the investment objectives.

Reserve funds may be invested in securities exceeding three years if the maturity of such investments are made to coincide as nearly as practicable with the expected use of the Funds. Any investment purchased with a maturity of four years must be supported with written documentation explaining the reason for the purchase and must be specifically approved by the City Council.

XI. Reporting

The Finance Director shall prepare as investment report at least quarterly, including a management summary that provides an analysis of the status of the current investment portfolio. This management summary will be prepared in a manner which will allow the City to ascertain whether investment activities during the reporting period have conformed to the Investment Policy. This report should be provided to the City Manager and the City Council and presented during a City Council Meeting. The report will include the following:

- Listing of individual securities held, by fund, at the end of the reporting period.
- Average weighted yield to maturity of portfolio.
- Listing of investments by maturity date.
- Percentage of total portfolio which each type of investment represents.

1. *Performance Standards*

The investment portfolio will be managed in accordance with the parameters specified within this Policy. The portfolio should obtain a market average rate of return during a market/economic environment of stable interest rates. Portfolio performance should be compared to appropriate benchmarks on a regular basis. The benchmarks shall be reflective of the actual securities being purchased and risks undertaken, and the benchmark shall have similar weighted average as the portfolio.

2. *Market Yield*

The City's investment strategy is passive. Given this strategy, the basis used by the Finance Director to determine whether market yield are being achieved shall be the six-month U.S. Treasury Bill.

3. *Marking to Market*

The market value of the portfolio shall be calculated at least quarterly and a statement of the market value of the portfolio shall be issued at least quarterly. This will ensure that review of the investment portfolio, in terms of value and price volatility, has been performed consistent with the GFOA recommended Practices on “Mark-to-Market Practices for State and Local Government Investment Portfolios and Investment Pools” (http://www.gfoa.org/best-practices). In defining market value, considerations should be given to the GASB Statement 31 pronouncement.

XII. Legislation and Documentation

The City's investment program shall comply at all times with the Illinois Public Funds Investment Act (30 ILCS 235/1 et seq.) and other state laws governing the investment of public funds, as amended from time to time. In an event of any conflict between this Policy and the Illinois Public Funds Investment Act and other state laws, the provisions in the Illinois Public Funds Investment Act and other state laws shall control the investment activities of the City.

The Finance Director will maintain a list and is hereby authorized to deposit City monies in accordance with 65 ILCS 5/3.1-35-50, in financial institutions as attached to hereto as Appendix A. The Finance Director shall review this list from time-to-time and shall submit any modifications to the City Council for approval. During the annual audit process, the City's Auditors will review the list of deposits and confirm the deposit amounts held at these financial institutions.

XIII. Policy Considerations

1. *Amendments*
This policy shall be reviewed on an annual basis by the Finance Director. Any changes must be submitted by the Finance Director to the City Manager with final approval by the City Council.

XIV. Approval of Investment Policy

The Investment Policy shall be formally approved and adopted by the City Council.

APPENDIX A: Listing of Authorized Financial Institutions

List of Depositories
J.P. Morgan Chase Bank

List of Investment Advisors
J.P. Morgan Chase Bank
PMA Securities, Inc.

List of Broker/Dealers
J.P. Morgan Securities LLC
PMA Securities, Inc.

List of Local Government Investment Pools
Illinois Funds
Illinois Trust
Illinois Metropolitan Investment Fund (IMET)

APPENDIX B: Glossary of Terms

AGENCIES: Informal name that refers to securities issued by the United States government and U.S. government sponsored instrumentalities.

ASK PRICE: The trading price proposed by the prospective seller of securities. Also called the offer or offered price.

BANKERS' ACCEPTANCE (BA): A short-term financial instrument that is the unconditional obligation of the accepting bank.

BASIS POINT (BP): A unit of measurement for interest rates or yields that are expressed in percentages. (One hundred basis points equal 1 percent.)

BID: The trading price acceptable to a prospective buyer of securities.

BOND EQUIVALENT YIELD (BEY): An annual yield, expressed as a percentage, describing the return provided to bond holders. The BEY is a way to compare yields available from discount securities such as Treasury bills and BAs with yields available from coupon securities.

BROKER: A party who brings buyers and sellers together. Brokers do not take ownership of the property being traded. They are compensated by commissions. They are not the same as dealers; however, the same individuals and firms that act as brokers in some transactions may act as dealers in other transactions.

BROKERED AND NEGOTIABLE CERTIFICATES OF DEPOSIT: Short-term (2 to 52 weeks) large denomination ($100,000 minimum). Certificate of Deposit that is issued at a discount on its par value, or at a fixed interest rate payable at maturity and are freely traded in secondary markets.

CERTIFICATE OF DEPOSIT (CD): A deposit of funds, in a bank or savings and loan association, for a specific term that earns interest at a specified rate or rate formula. CDs may be secured or unsecured, may be in negotiable or nonnegotiable form and may be issued in either physical or book entry form.

COLLATERAL: Process by which a borrower pledges securities, property or other deposits for the purpose of securing the repayment of a loan and/or security.

COMMERCIAL PAPER (CP): Unsecured, short-term promissory notes issued by corporations for specific amounts and with specific maturity dates ranging from 2 to 270 days.

COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR): The official annual audit report for the City. It includes five combined statements and basic financial statements for each individual fund and account group prepared in conformity with GAAP. It also includes supporting schedules necessary to demonstrate compliance with finance-related legal and contractual provisions, extensive introductory material, and a detailed Statistical Section.

COUPON: (a) The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value.
(b) A certificate attached to a bond evidencing interest due on a payment date.

CREDIT RISK: The risk to an investor that in 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 firm or individual who buys and sells for their own account. Dealers have ownership between a purchase from one party and a sale to another party. Dealers are compensated by the spread between the price they pay and the price they receive.

DEBENTURE: A bond secured only by the general credit of the issuer.

DELIVERY VERSUS PAYMENT (DVP): The simultaneous exchange of securities and cash. The safest method of settling either the purchase or sale of a security. In a DVP settlement, the funds are wired from the buyer's account and the security is delivered from the seller's account in simultaneous independent wires.

DISCOUNT: The amount by which the price for a security is less than its par.

DISCOUNT SECURITIES: Securities that do not pay periodic interest. Investors earn the difference between the discount issue price and the full face value paid at maturity. Treasury bills, bankers' acceptances and zero coupon bonds are discount securities.

DIVERSIFICATION: A process of investing assets among a range of security types by sector, maturity and quality rating.

DURATION: A measure of the timing of cash flows, such as the interest payments and the principal repayment, to be received from a given-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.

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 OF INSURANCE CORPORATION (FDIC): A federal agency that insures bank deposits, currently up to $250,000 per deposit.

FEDERAL FUNDS RATE: The rate for which overnight federal funds are traded.

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-à-vis member commercial banks.

FEDERAL NATIONAL MORTGAGE ASSOCIATION (FNMA or FANNIE MAE): 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 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 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 rotation 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): GNMA, like FNMA, was chartered under the Federal National Mortgage Association Act of 1938. 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- throughs* is often used to describe Ginnie Maes.

LIQUIDITY: A liquid asset is one that can be readily converted to cash through sale in an active secondary market.

LOCAL GOVERNMENT INVESTMENT POOL (LGIP): Pools through which governmental entities may invest short term cash. Examples of LGIP's are the Illinois Funds, administered by the Illinois State Treasurer and the Illinois Metropolitan Investment Fund.

MARKET VALUE: The price at which a security could presumably be purchased or sold.

MARK TO MARKET: The process of restating the carrying value of an asset or liability to equal its current market value.

MARKET RISK: The risk that the value of a security will rise or decline as a result of changes in market conditions.

MASTER REPURCHASE AGREEMENT: A written contract covering all future transactions between parties. The agreement establishes each party's right in the transaction. Repurchase Agreements (REPO's) are a form of short-term borrowing for dealers in government securities. The dealer sells the government securities to investors, usually on an overnight basis, and then buys them back the following day. For the party selling the security (and agreeing to repurchase it in the future), it is a repo; for the party on the other end of the transaction (buying the security and agreeing to sell in the future), it is a reverse repurchase agreement. A master agreement will often specify, among other things, the right to liquidate the underlying securities in the event of default.

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

MONEY MARKET: The aggregation of buyers and sellers actively trading money market instruments.

OFFER OF OFFERED PRICE: The trading price proposed by the prospective seller of securities (also called the asked or asking price).

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.

PORTFOLIO: Collection of financial assets belonging to a single owner.

PREMIUM: The amount by which the price for a security is greater than its par amount.

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 unrelated firms.

PRUDENT PERSON RULE: An investment standard. In some states the law requires that a fiduciary, such as a trustee, may invest money only in a list of securities selected by the state - the so-called *legal list*. In 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.

REINVESTMENT RISK: The risk that all or part of the principal may be received when interest rates are lower than when the security was originally purchased, so that the principal must be reinvested at a lower rate than the rate originally received by the investor.

REPURCHASE AGREEMENT (RP OR REPO): See Master Repurchase Agreement.

SAFEKEEPING: A service rendered by banks whereby securities and valuables of all types and descriptions are held by the bank.

SEC RULE 15C3-1: See uniform net capital rule.

SECONDARY MARKET: Markets for the purchase and sale of any previously issued financial instrument.

SECURITIES & EXCHANGE COMMISSION (SEC): The federal agency with responsibility for regulating financial exchanges for cash instruments.

SPREAD OVER TREASURIES: The difference between the bond equivalent yield for any investment and the bond equivalent yield for a Treasury investment with the same maturity.

TREASURY BILLS (T-BILLS): Short-term obligations issued by the U.S. Treasury for maturities of one year or less. They do not pay interest but are issued on a discount basis instead.

TREASURY BONDS (T-BONDS): Long-term obligations issued by the U.S. Treasury with initial maturities of more than ten years.

TREASURY NOTES (T-NOTES): Medium-term obligations issued by the U.S. Treasury with initial maturities of from one to ten years.

UNIFORM NET CAPITAL RULE: Securities and Exchange Commission requirement that member firms as well as non- member 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 syndicate. *Liquid capital* includes cash and assets easily converted to cash.

WEIGHTED AVERAGE MATURITY: The average maturity of all the securities that comprise a portfolio.

YIELD: Loosely refers to the annual return on an investment expressed as a percentage on an annual basis. For interest- bearing securities, the yield is a function of the rate, the purchase price, the income that can be earned from the reinvestment of income received prior to maturity, call or sale. Different formulas or methods are used to calculate yield.