



**FARMERS  
BRANCH**

**RESOLUTION NO. 2014-065**

**A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF FARMERS BRANCH, TEXAS, AMENDING THE CITY OF FARMERS BRANCH INVESTMENT POLICY ATTACHED HERETO AS EXHIBIT "A"; DECLARING THAT THE CITY COUNCIL HAS COMPLETED ITS REVIEW OF THE INVESTMENT POLICY OF THE CITY AND THAT EXHIBIT "A" RECORDS ANY CHANGES TO THE INVESTMENT POLICY; PROVIDING A REPEALING CLAUSE; PROVIDING A SEVERABILITY CLAUSE; AND PROVIDING FOR AN EFFECTIVE DATE.**

**WHEREAS**, in accordance with the Public Funds Investment Act, Chapter 2256, Texas Government Code, the City Council of the City of Farmers Branch, Texas by resolution adopted an investment policy; and,

**WHEREAS**, Section 2256.005, Texas Government Code requires the City Council to review the investment policies and investment strategies not less than annually and to adopt a resolution or order stating the review has been completed and record any changes made to either the investment policies or investment strategies.

**NOW THEREFORE, BE IT RESOLVED, BY THE CITY COUNCIL OF THE CITY OF FARMERS BRANCH, TEXAS THAT:**

**SECTION 1.** The City's Investment Policy, attached as Exhibit "A", is hereby adopted and shall govern the investment policies for the City, and shall define the authority of the investment official of the City from and after the effective date of this resolution.

**SECTION 2.** The City Council of the City of Farmers Branch has completed its review of the investment policies and investment strategies and any changes made to either the investment policies or investment strategies are recorded in Exhibit "A" hereto.

**SECTION 3.** All provisions of the resolutions of the City of Farmers Branch, Texas, in conflict with the provisions of this resolution be, and the same are hereby, repealed, and all other provisions not in conflict with the provisions of this resolution shall remain in full force and effect.

**SECTION 4.** Should any word, sentence, paragraph, subdivision, clause, phrase or section of this resolution be adjudged or held to be void or unconstitutional, the same shall not affect the validity of the remaining portions of said resolution which shall remain in full force and effect.

**SECTION 5.** This resolution shall become effective immediately from and after its passage.

**PASSED AND APPROVED BY THE CITY COUNCIL OF THE CITY OF FARMERS  
BRANCH, TEXAS, THIS 16<sup>th</sup> DAY OF SEPTEMBER 2014.**

**ATTEST:**

**APPROVED:**

\_\_\_\_\_  
Angela Kelly, City Secretary

\_\_\_\_\_  
Bob Phelps, Mayor

**APPROVED AS TO FORM:**

\_\_\_\_\_  
Peter G. Smith, City Attorney  
(Routine)

*Exhibit "A"*

**CITY OF FARMERS BRANCH  
INVESTMENT POLICY  
INTRODUCTION**

The purpose of this document is to set forth specific investment policy and strategy guidelines for the City of Farmers Branch in order to achieve the goals of safety, liquidity, yield, and public trust for all investment activity. The City Council of the City of Farmers Branch shall review and adopt, by resolution, its investment strategies and policy not less than annually. The resolution shall include a record of changes made to either the investment policy or strategy. This policy serves to satisfy the statutory requirement (specifically the Public Funds Investment Act, Article 342a-2 V.T.C.S. (the "Act")) to define, adopt and review a formal investment strategy and policy.

**INVESTMENT STRATEGY**

The City of Farmers Branch maintains portfolios that utilize four specific investment strategy considerations designed to address the unique characteristics of the fund groups represented in the portfolios:

- A. Investment strategies for operating funds and commingled pools containing operating funds have as their primary objective to assure that anticipated cash flows are matched with adequate investment liquidity. The secondary objective is to create a portfolio structure that will experience minimal volatility during economic cycles. This may be accomplished by purchasing high quality, short to medium-term securities that will complement each other in a laddered or barbell maturity structure. The dollar weighted average maturity will be calculated using the stated final maturity date of each security.
- B. Investment strategies for debt service funds shall have as the primary objective the assurance of investment liquidity adequate to cover the debt service obligation on the required payment date. Securities purchased shall not have a stated final maturity date which exceeds the debt service payment date.
- C. Investment strategies for debt service reserve funds shall have as the primary objective the ability to generate a dependable revenue stream to the appropriate debt service fund from securities with a low degree of volatility. Securities should be of high quality and, except as may be required by the bond ordinance specific to an individual issue, of short to intermediate-term maturities. Volatility shall be further controlled through the purchase of securities carrying the highest coupon available, within the desired maturity and quality range, without paying a premium, if at all possible.

Investment strategies for special projects or special purpose fund portfolios will have as their primary objective to assure that anticipated cash flows are matched with adequate

investment liquidity. These portfolios should include at least 10% in highly liquid securities to allow for flexibility and unanticipated project outlays. The stated final maturity dates of securities held should not exceed the estimated project completion date.

## **INVESTMENT POLICY**

### **I. SCOPE**

This investment policy applies to all financial assets of the City of Farmers Branch. These funds are accounted for in the City's Comprehensive Annual Financial Report (CAFR) and include:

- \* General Fund
- \* Special Revenue Funds
- \* Debt Service Funds
- \* Capital Projects Funds
- \* Proprietary Funds
- \* All Other Funds

### **II. OBJECTIVES**

The City of Farmers Branch shall manage and invest its cash with four objectives, listed in order of priority: Safety, Liquidity, Yield, and Public Trust. The safety of the principal invested always remains the primary objective. All investments shall be designed and managed in a manner responsive to the public trust and consistent with State and Local law.

The City shall maintain a comprehensive cash management program that includes collection of accounts receivable, vendor payment in accordance with invoice terms, and prudent investment of available cash. Cash management is defined as the process of managing monies in order to insure maximum cash availability and maximum yield on short-term investment of pooled idle cash.

#### **Safety**

The primary objective of the City's investment activity is the preservation of capital in the overall portfolio. Each investment transaction shall be conducted in a manner to avoid capital losses, whether they are from securities defaults or erosion of market value.

#### **Liquidity**

The City's investment portfolio shall be structured such that the City is able to meet all obligations in a timely manner. This shall be achieved by matching investment maturities with forecasted cash flow requirements and by investing in securities with active secondary markets.

## Yield

The City's cash management portfolio shall be designed with the objective of regularly exceeding the average rate of return on U.S. Treasury Bills at a maturity level comparable to the City's weighted average maturity in days. The investment program shall seek to augment returns above this threshold consistent with risk limitations identified herein and prudent investment policies.

## Public Trust

All participants in the City's investment process shall seek to act responsibly as custodians of the public trust. Investment officials shall avoid any transaction that might impair public confidence in the City's ability to govern effectively.

# **III. RESPONSIBILITY AND CONTROL**

## Investment Committee

An Investment Committee, consisting of the City Manager, the Managing Director of Finance & Administration, Chief Accountant, and Financial Analyst shall meet at least quarterly to determine operational strategies and to monitor results. The Investment Committee shall include in its deliberation such topics as: performance reports, economic outlook, portfolio diversification, maturity structure, potential risk to the City's funds, authorized brokers and dealers, and the target rate of return on the investment portfolio.

## Delegation of Authority and Training

Authority to manage the City's investment program is derived from a resolution of the City Council. The Managing Director of Finance & Administration is designated as investment officer of the City and is responsible for investment decisions and activities. The Managing Director of Finance & Administration shall establish written procedures for the operation of the investment program, consistent with this investment policy. The investment officer shall attend at least one 10-hour training session relating to the officer's responsibility under the Act within 12 months after assuming duties. Thereafter, the investment officer shall attend a 10-hour training session not less than once every two years. Such training from an independent source shall be approved or endorsed by the Government Finance Officers Association of Texas, the Government Treasurers Organization of Texas, the Texas Municipal League, or the North Central Texas Council of Governments.

## Internal Controls

The Managing Director of Finance & Administration is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the entity are protected from loss, theft or misuse. The internal control structure shall be 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.

Accordingly, the Managing Director of Finance & Administration shall establish a process for annual independent review by an external auditor to assure compliance with policies and procedures. The results of this review shall be reported to the City Council. The internal controls shall address the following points:

- A. Control of collusion. Collusion is a situation where two or more employees are working in conjunction to defraud their employer.
- B. 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.
- C. 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.
- D. 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.
- E. 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.
- F. Written confirmation for telephone (voice) transactions for investments and wire transfers. Due to the potential for error and improprieties arising from telephone transactions, all telephone transactions should be supported by written communications and approved by the appropriate person. Written communications may be via facsimile if on letterhead and the safekeeping institution has a list of authorized signatures.
- G. Development of a wire transfer agreement with the depository bank or third party custodian. This agreement should outline the various controls, security provisions, and delineate responsibilities of each party making and receiving wire transfers.

### Prudence

The standard of prudence to be applied by the investment officer shall be the "prudent investor" rule, which states: "Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived." In determining whether an investment officer has exercised prudence with respect to an investment decision, the determination shall be made taking into consideration:

- A. The investment of all funds, or funds under the City's control, over which the officer had responsibility rather than a consideration as to the prudence of a single investment.

- B. Whether the investment decision was consistent with the written investment policy of the City.

The investment officer, acting in accordance with written procedures and exercising due diligence, shall not be held personally responsible for a specific security's credit risk or market price changes, provided that these deviations are reported immediately and that appropriate action is taken to control adverse developments.

#### Ethics and Conflicts of Interest

City staff 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 the ability to make impartial investment decisions. City staff shall disclose to the City Manager any material financial interests in financial institutions that conduct business with the City and they shall further disclose positions that could be related to the performance of the City's portfolio. City staff shall subordinate their personal financial transactions to those of the City, particularly with regard to timing of purchases and sales.

An investment officer of the City who has a personal business relationship with an organization seeking to sell an investment to the City shall file a statement disclosing that personal business interest. An investment officer who is related within the second degree by affinity or consanguinity to an individual seeking to sell an investment to the City shall file a statement disclosing that relationship. A statement required under this subsection must be filed with the Texas Ethics Commission and the governing body of the entity.

### **IV. REPORTING**

#### Quarterly Reporting

The Managing Director of Finance & Administration shall submit a signed quarterly investment report that summarizes current market conditions, economic developments and anticipated investment conditions. The report shall summarize investment strategies employed in the most recent quarter, and describe the portfolio in terms of investment securities, maturities, risk characteristics, current credit rating, and shall explain the total investment return for the quarter.

#### Annual Report

Within 60 days of the end of the fiscal year, the Managing Director of Finance & Administration shall present an annual report on the investment program and investment activity. This report may be presented as a component of the fourth quarter report to the City Manager and City Council.

#### Methods

The quarterly investment report shall include a succinct management summary that provides a clear picture of the status of the current investment portfolio and transactions made over the last quarter. This management summary will be prepared in a manner that will allow the City to ascertain whether investment activities during the reporting period have conformed to the

investment policy. The report will be prepared in compliance with generally accepted accounting principles. The report will be provided to the City Manager and City Council. The report will include the following:

- A. A listing of individual securities, including credit rating, held at the end of the reporting period. This list will include the name of the fund or pooled group fund for which each individual investment was acquired.
- B. Unrealized gains or losses resulting from appreciation or depreciation by listing the beginning and ending book and market value of securities for the period. Market values shall be obtained from financial institutions or portfolio reporting services independent from the broker/dealer from whom the security was purchased.
- C. Additions and changes to the market value during the period.
- D. Fully accrued interest for the reporting period.
- E. Average weighted yield to maturity of portfolio on entity investments as compared to applicable benchmarks.
- F. Listing of investments by maturity date.
- G. The percentage of the total portfolio that each type of investment represents.
- H. Statement of compliance of the City's investment portfolio with State Law and the investment strategy and policy approved by the City Council.

## **V. INVESTMENT PORTFOLIO**

### **Active Portfolio Management**

The City shall pursue an active versus a passive portfolio management philosophy. That is, securities may be sold before they mature if market conditions present an opportunity for the City to benefit from the trade. The investment officer will routinely monitor the contents of the portfolio, the available markets, and the relative value of competing instruments, and will adjust the portfolio accordingly.



## Investments

Assets of the City of Farmers Branch may be invested in the following instruments; provided, however, that at no time shall assets of the City be invested in any instrument or security not authorized for investment under the Act, as the Act may from time to time be amended. The City is not required to liquidate investments that were authorized investments at the time of purchase.

### I. Authorized

- A. Obligations of the United States of America, its agencies and instrumentalities, which have a liquid market with a readily determinable market value.
- B. Direct obligations of the State of Texas and agencies thereof.
- C. Other obligations, the principal of and interest on which are unconditionally guaranteed by the State of Texas or United States of America.
- D. Obligations of the States, agencies thereof, Counties, Cities, and other political subdivisions of any state having been rated as investment quality by a nationally recognized investment rating firm, and having received a rating of not less than "A" or its equivalent.
- E. Certificates of Deposit of state and national banks domiciled in Texas, guaranteed or insured by the Federal Deposit Insurance or its successor or secured by obligations described in A through D above, which are intended to include all direct agency or instrumentality issued mortgage backed securities rated AAA by a nationally recognized rating agency, or by Article 2529b-1, V.T.C.S., and that have a market value of not less than the principal amount of the certificates.
- F. Fully collateralized direct repurchase agreements with a defined termination date secured by obligations of the United States or its agencies and instrumentalities pledged with a third party, selected by the Managing Director of Finance & Administration, other than an agency for the pledgor. Repurchase agreements must be purchased through a primary government securities dealer, as defined by the Federal Reserve, or a bank domiciled in Texas. A Master Repurchase Agreement must be signed by the bank/dealer prior to investment in a repurchase agreement.
- G. Joint pools of political subdivisions in the State of Texas which invest in instruments and follow practices allowed by current law. Investment in such pools shall be limited to 15% of the City's entire portfolio. A pool must be continuously rated no lower than AAA or AAA-m or at an equivalent rating by a least one nationally recognized rating service.

## II. Not Authorized

The City's authorized investments options are more restrictive than those allowed by State law. State law specifically prohibits investment in the following investment securities.

- A. Obligations whose payment represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pays no principal.
- B. Obligations whose payment represents the principal stream of cash flow from the underlying mortgage-backed security collateral and bears no interest.
- C. Collateralized mortgage obligations that have a stated final maturity date of greater than 10 years.
- D. Collateralized mortgage obligations the interest rate of which is determined by an index that adjusts opposite to the changes in a market index.

### Holding Period

The City of Farmers Branch intends to match the holding periods of investment funds with liquidity needs of the City. In no case will the average maturity of investments of the City's operating funds exceed 18 months. For operating funds and commingled pools containing operating funds of the City, the maximum final stated maturity of any investment shall not exceed five years.

Investments in all funds shall be managed in such a way that the market price losses resulting from interest rate volatility would be offset by coupon income and current income received from the volume of the portfolio during a twelve month period.

### Risk and Diversification

The City of Farmers Branch recognizes that investment risks can result from issuer defaults, market price changes or various technical complications leading to temporary illiquidity. Risk is controlled through portfolio diversification, which shall be achieved by the following general guidelines:

- A. Risk of issuer default is controlled by limiting investments to those instruments allowed by the Act, which are described herein.
- B. Risk of market price changes shall be controlled by avoiding over-concentration of assets in a specific maturity sector, limitation of average maturity of operating funds investments to one year, and avoidance of over-concentration of assets in specific instruments other than U.S. Treasury Securities and Insured or Collateralized Certificates of Deposits.

- C. Risk of illiquidity due to technical complications shall be controlled by the selection of securities dealers as described herein.

## **VI. SELECTION OF BANKS AND DEALERS**

### Depository

At least every five years a Depository shall be selected through the City's banking services procurement process, which shall include a formal request for proposal (RFP). In selecting a depository, the credit worthiness of institutions shall be considered, and the Managing Director of Finance & Administration shall conduct a comprehensive review of prospective depository's credit characteristics and financial history.

### Certificates of Deposit

Banks seeking to establish eligibility for the City's competitive certificate of deposit purchase program shall submit for review annual financial statements, evidence of federal insurance and other information as required by the Managing Director of Finance & Administration.

### Securities Dealers

For brokers and dealers of government securities, the City shall select only those dealers reporting to the Market Reports Division of the Federal Reserve Board of New York, also known as the "Primary Government Security Dealers." unless a comprehensive credit and capitalization analysis reveals that other firms are adequately financed to conduct public business. Only brokers and dealers with a Dallas, Texas or Farmers Branch, Texas office shall be selected. Investment officials shall not knowingly conduct business with any firm with whom public entities have sustained losses on investments. All Securities dealers shall provide the City with references from public entities, which they are currently serving. The Investment Committee shall adopt and annually review a list of qualified brokers authorized to engage in investment transactions with the entity.

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

- audited financial statements
- proof of National Association of Securities Dealers (NASD) certification
- proof of state registration
- completed broker/dealer questionnaire
- certification of having read the City's investment policy signed by a qualified representative of the organization
- acknowledgment that the organization has implemented reasonable procedures and controls in an effort to preclude imprudent investment activities arising out of investment transactions conducted between the City and the organization

Qualified representative means a person who holds a position with a business organization, who is authorized to act on behalf of the business organization, and who is one of the following:

- A. For a business organization doing business that is regulated by or registered with a securities commission, a person who is registered under the rules of the National Association of Securities Dealers;
- B. For a state or federal bank, a savings bank, or a state or federal credit union, a member of the loan committee for the bank or branch of the bank or a person authorized by corporate resolution to act on behalf of and bind the banking institution; or
- C. For an investment pool, the person authorized by the elected official or board with authority to administer the activities of the investment pool to sign the certification on behalf of the investment pool.

### Investment Pools

A thorough investigation of the pool is required prior to investing, and on a continual basis. All investment pools must supply the following information in order to be eligible to receive funds:

- \* the types of investments in which money is allowed to be invested
- \* the maximum average dollar-weighted maturity allowed, based on the stated maturity date, of the pool
- \* the maximum stated maturity date any investment security within the portfolio has
- \* the objectives of the pool
- \* the size of the pool
- \* the names of the members of the advisory board of the pool and the dates their terms expire
- \* the custodian bank that will safekeep the pool's assets
- \* whether the intent of the pool is to maintain a net asset value of one dollar and the risk of market price fluctuation
- \* whether the only source of payment is the assets of the pool at market value or whether there is a secondary source of payment, such as insurance or guarantees, and a description of the secondary source of payment
- \* the name and address of the independent auditor of the pool
- \* the requirements to be satisfied for an entity to deposit funds in and withdraw funds from the pool and any deadlines or other operating policies required for the entity to invest funds in and withdraw funds from the pool
- \* the performance history of the pool, including yield, average dollar-weighted maturities, and expense ratios
- \* a description of interest calculations and how interest is distributed, and how gains and losses are treated.

An annual review of the financial condition and registration of qualified bidders will be conducted by the Managing Director of Finance & Administration.

## **VII. SAFEKEEPING AND CUSTODY**

### Insurance or Collateral

All deposits and investments of City funds other than direct purchases of U.S. Treasuries or Agencies shall be secured by pledged collateral. In order to anticipate market changes and provide a level of security for all funds, the collateralization level will be 102% of market value of principal and accrued interest on the deposits or investments less an amount insured by the FDIC or FSLIC. Evidence of the pledged collateral shall be maintained by the Managing Director of Finance & Administration or a third party financial institution. Repurchase agreements shall be documented by a specific agreement noting the collateral pledge in each agreement. Collateral shall be reviewed weekly to assure that the market value of the pledged securities is adequate.

### Safekeeping Agreement

Collateral pledged to secure deposits of the City shall be held by a *third-party* safekeeping institution in accordance with a Safekeeping Agreement which clearly defines the procedural steps for gaining access to the collateral should the City of Farmers Branch determine that the City's funds are in jeopardy. The safekeeping institution, or Trustee, shall be the Federal Reserve Bank or an institution not affiliated with the firm pledging the collateral. The safekeeping agreement shall include the signatures of authorized representatives of the City of Farmers Branch, the firm pledging the collateral, and the Trustee.

### Collateral Defined

The City of Farmers Branch shall accept only the following securities as collateral:

- A. FDIC and FSLIC insurance coverage.
- B. A bond, certificate of indebtedness, or Treasury Note of the United States, or other evidence of indebtedness of the United States that is guaranteed as to principal and interest by the United States.
- C. Obligations, the principal and interest on which, are unconditionally guaranteed or insured by the State of Texas.
- D. A bond of the State of Texas or of a county, city or other political subdivision of the State of Texas having been rated as investment grade (investment rating no less than "A" or its equivalent) by a nationally recognized rating agency with a remaining maturity of ten (10) years or less.
- E. A surety bond (issued by a solvent surety company authorized to do business in Texas) rated no less than "AAA" or its equivalent by a nationally recognized rating agency.

### Subject to Audit

All collateral shall be subject to inspection and audit by the Managing Director of Finance & Administration or the City's independent auditors.

### Delivery vs. Payment

Treasury Bills, Notes, Bonds, Repurchase Agreements and Government Agencies' securities shall be purchased using the delivery vs. payment method. That is, funds shall not be wired or paid until verification has been made that the correct security was received by the Trustee. The security shall be held in the name of the City or held on behalf of the City. The Trustee's records shall assure the notation of the City's ownership of or explicit claim on the securities. The original copy of all safekeeping receipts shall be delivered to the City.

## **VIII. INVESTMENT POLICY ADOPTION**

The City of Farmers Branch investment policy shall be adopted by resolution of the City Council. The policy shall be reviewed for effectiveness on an annual basis by the Investment Committee and any modifications will be recommended for approval to the City Council. The City Council shall review these investment policies and strategies not less than annually.

## GLOSSARY OF COMMON TREASURY TERMINOLOGY

**Agencies:** Federal agency securities.

**Asked:** The price at which securities are offered.

**Bid:** 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 position. In the money market, brokers are active in markets in which banks buy and sell money and in interdealer markets.

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

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

**Comprehensive Annual Financial Report (CAFR):** The official annual report for the City of Farmers Branch. 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.

**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 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:** Dividing investment funds among a variety of securities offering independent returns.

**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 Fed 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-à-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 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.

**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 prices 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:** To protect investors, many public investors will request that repurchase agreements be preceded by a master repurchase agreement between the investor and the financial institution or dealer. The master agreement should define the nature of the transaction, identify the relationship between the parties, establish normal practices regarding ownership and custody of the collateral securities during the term of the investment, provide remedies in the case of default by either party, and clarify issues of ownership. The master repurchase agreement protects the investor by eliminating the uncertainty of ownership and hence, allowing investors to liquidate collateral if a bank or dealer defaults during the term of the agreement.

**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.

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

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

**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.

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

**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.

**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 from one to ten years.

**Yield:** The rate of annual income return on an investment, expressed as a percentage. (a) **Income Yield** is obtained by dividing the current dollar income by the current market price of the security. (b) **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.

**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.