ITEM # 12
DATE: 07-31-18

COUNCIL ACTION FORM

SUBJECT: **CITY OF AMES INVESTMENT POLICY**

BACKGROUND:

The Code of Iowa Section 12B.10B requires the City Council to adopt a written investment policy. The policy sets guidance for investment of City funds, and staff reports to City Council on compliance with the policy on a quarterly basis. City staff periodically reviews the investment policy and submits revisions for approval. The current City of Ames Investment Policy was last revised in July of 2007. **A summary of changes recommended in the proposed revision to the policy includes:**

- Clarified wording throughout the policy to comply with the Code of Iowa.
- Inserted wording in Section 2.0 to include achieving maximum security through diversification and adherence to the City's objectives.
- Inserted wording in Section 5.2 to clarify that employees and investment officials shall disclose to the City Manager's office any material interests in financial institutions with which they conduct business.
- Inserted wording in Section 18.1 to clarify that the City Treasurer shall prepare an investment report quarterly and present to the City Council within 45 days of each quarters end.
- Updated the Appendix to show that FDIC insurance is now $250,000 per deposit.

As part of the current review, a draft of the revised investment policy was forwarded to the Association of Public Treasurers of United States and Canada (APT-US&C) for review and certification. **The APT-US&C Investment Policy Certification Committee has approved the revised City of Ames Investment Policy for the Investment Policy Certificate of Excellence Award.** The City of Ames will receive an award plaque at the APT-US&C Annual Conference in July. The APT-US&C's Certification Program provides guidance and assistance in developing or improving investment policies in the public sector.

ALTERNATIVES:

1. Adopt the revised City of Ames Investment Policy.

2. Refer the City of Ames Investment Policy to staff for further revision.

MANAGER'S RECOMMENDED ACTION:

The revised City of Ames Investment Policy establishes guidelines in accordance with best policy practices. The Investment Policy has been updated to reflect the current Code of Iowa requirements.

Therefore, it is the recommendation of the City Manager that the City Council adopt Alternative No.1, thereby adopting the revised City of Ames Investment Policy.

CITY OF AMES

INVESTMENT POLICY

Revised April 2018

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CITY OF AMES, IOWA
INVESTMENT POLICY

1.0 PURPOSE

The purpose of this investment policy is to set investment objectives, policies, establish guidelines, and define responsibilities for the investment of funds for the City of Ames.

2.0 POLICY

The policy of the City of Ames is to invest all funds in a manner that will provide the highest investment return while meeting cash flow demands and maintaining maximum security through diversification and adherence to the City's objectives. This policy is intended to comply with the <u>Code of Iowa</u> for investment of public funds.

This policy is static and general in nature; it defines authorized investments and guides the investment decisions and security selection process. The City's Investment Policy will be regularly reviewed and adjusted to create a portfolio that is suitable for the City given current conditions.

3.0 SCOPE

This investment policy applies to all funds and investment transactions of the City. These funds are accounted for in the Comprehensive Annual Financial Report, which includes the following:

3.1 General Fund
3.2 Special Revenue Funds
3.3 Capital Projects Funds (includes restricted bond proceeds)
3.4 Enterprise Funds (includes restricted sinking funds)
3.5 Trust and Agency Funds
3.6 Internal Service Funds
3.7 Any new fund created by the City of Ames, unless specifically exempted

The restricted sinking funds and bond proceeds are invested in compliance with this investment policy and applicable bond resolutions.

Individual employee retirement funds and deferred compensation are excluded from this policy.

3.8 <u>Pooling of Funds</u>
Except for cash in certain restricted and special funds, the City of Ames will consolidate cash balances from all funds to maximize investment earnings and to increase efficiencies with regard to investment pricing, safekeeping

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

4.0 OBJECTIVES

The primary objectives, in priority order, for the City of Ames investment activities shall be safety, liquidity, and yield:

4.1 Safety

With safety being the foremost objective, care must be taken to ensure the preservation of capital and the protection of principal. The objective will be to mitigate credit risk and interest rate risk by following the guidelines listed below.

a. Credit Risk

The City of Ames will minimize credit risk (the risk of loss due to the failure of the security issuer or backer) by:

- Limiting investments to those addressed in Section 10.0 of this investment policy.
- Pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisors with whom the City will do business.
- Diversifying the investment portfolio by agency and issuer so that potential losses on individual securities can be minimized.
- Holding a minimum of 5% of the total portfolio in highly marketable short-term treasuries, checking with interest, government pooled account, or a combination of all three.

b. Interest Rate Risk

The City of Ames 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 securities mature to meet cash requirements for operations, thereby avoiding the need to sell securities in the open market prior to maturity.
- Purchasing investments with the intent to hold until maturity.
- Investing operating funds primarily in shorter-term securities, money market mutual funds, or similar investment pools and limiting the average maturity of the portfolio in accordance with this policy (see Section 17.1).

4.2 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.

4.3 Yield

The portfolio shall be designed to obtain a reasonable rate of return throughout budgetary and economic cycles. The return on investments is to be accorded secondary importance compared to the safety and liquidity objectives described above. The core of investments will focus on relatively low risk securities with an expectation of earning a reasonable return relative to the risk being assumed. Securities shall not be sold prior to maturity, with the following exceptions:

- A security with declining value may be sold early to minimize loss of principal.
- A security may be exchanged to improve the quality, yield, or target duration in the portfolio.
- A security may be sold in order to satisfy liquidity requirements.

When selling a security prior to maturity, the City Treasurer must be prepared to justify the reasons and explain any gains or losses.

It is important to remember that compliance with the policy does not measure return, but rather manages risk. Policy compliance does not provide a benchmark to meet or exceed, but is a model to follow. The City will benchmark its portfolio performance to the appropriate “treasuries constant maturity” rate based on portfolio maturities of the investment plan.

5.0 STANDARDS OF CARE

5.1 Prudence

The standard of prudence to be used by investment officials shall 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 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.

The "prudent person" standard states that, "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."

5.2 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 to the City Manager's office any material interests in financial institutions with which they conduct business. 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 Ames.

The City investment program shall be managed in a professional and prudent manner worthy of the public trust and review.

6.0 INVESTMENT AUTHORITY AND RESPONSIBILITY

6.1 Authority

In accordance with Section 12B.10 of the Code of Iowa, the responsibility for conducting investment transactions resides with the City Treasurer. The City Treasurer, under the general direction of the City Council, shall be responsible for all transactions undertaken and shall establish a system of controls to regulate activities.

The Code of Iowa Section 12B.10B requires the City governing body to adopt a written investment policy and distribute copies to the following:

- The governing body or officer of the City of Ames to which the policy applies.
- All depository institutions or fiduciaries for public funds of the City of Ames.
- The external auditor engaged to audit any fund of the City of Ames.

6.2 Responsibility Assigned

The City Treasurer shall invest all funds for the City in accordance with the investment policy. In the absence of the City Treasurer, authority is delegated first to the Director of Finance, and then to the Assistant City Manager with supervision responsibility over the Finance Department. All designees shall act in accordance with the established policies and internal controls set forth in the investment policy.

7.0 INVESTMENT PROCEDURES

The City Treasurer shall establish written investment procedures consistent with this investment policy for the operation of the investment program. Procedures should include references to: safekeeping, delivery vs. payment, investment accounting, repurchase agreements, wire transfer agreements, internal controls, collateral/depository agreements, daily cash flow review, basis for awarding bids, authorized personnel, and portfolio inventory.

The procedures document is intended to provide guidance for staff and to provide continuity in the event of an interruption of service of the City Treasurer.

8.0 AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS

8.1 Selection Process

A list of financial institutions authorized to provide investment services to the City of Ames will be maintained. In accordance with the Code of Iowa, this list will state the maximum authorized deposit amount allowed in each institution and must be approved by City Council.

In addition, a list of broker/dealers will be maintained. This list may include both primary and regional dealers. Dealers will be approved by the City Treasurer and the Director of Finance based on the following:

- Creditworthiness
- License to conduct business in Iowa
- Qualification under Securities and Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule)

8.2 Financial Institutions and Broker/Dealers

All financial institutions and broker/dealers who desire to conduct business with the City of Ames shall supply the City with the following:

- Audited financial statements, provided annually
- Trading resolutions
- Proof of state registration, if applicable
- Completed broker/dealer questionnaire
- Copy of the broker’s license for the individuals servicing the account
- Resume of individual servicing the account
- Any pending legal or regulatory sanctions
- Certification of having read and understood and agreeing to comply with the City of Ames investment policy
- Evidence of adequate insurance coverage

An annual review of the financial condition and registration of all qualified financial institutions and broker/dealers will be conducted by the City Treasurer.

9.0 SUITABILITY

Suitability, not simply return, is the standard for selecting investments for the portfolio. The City Treasurer shall review the following when selecting investments for the City:

- Sufficient liquidity to meet current obligations
- Appropriate level of market risk
- Diversified portfolio
- Legal investments
- Market rate of return

10.0 AUTHORIZED INVESTMENTS (Code of Iowa, Section 12.B10(5))

10.1 Permitted investments

- U.S. Treasury obligations which carry the full faith and credit guarantee of the United States Government and are considered to be the most secure instruments available.
- U.S. Government agency and instrumentality obligations that have a liquid market with a readily determinable market value.
- Certificates of deposit and other evidences of deposit at federally insured depository institutions approved pursuant to Chapter 12C, Code of Iowa.
- Certificate of Deposit Account Registry Service (CDARS) deposited with an authorized financial institution pursuant to Chapter 12B.10 (7), Code of Iowa.
- Prime bankers' acceptances that mature within two hundred seventy (270) days and that are eligible for purchase by a federal reserve bank, provided that at the time of purchase, no more than ten percent of the investment portfolio shall be in investments authorized by this paragraph and that at the time of purchase, no more than five percent of the investment portfolio shall be invested in the securities of a single issuer.
- Commercial paper or other short-term corporate debt that matures within 270 days and that is rated within the two highest classifications, as established by at least one of the standard rating services approved by the superintendent of banking by rule adopted pursuant to Chapter 17A, Code of Iowa, provided that at the time of purchase, no more than five percent of all amounts invested in commercial paper and other short-term corporate debt shall be invested in paper and debt rated in the second highest classification, and provided further that at the time of purchase, no more than ten percent of the investment portfolio shall be in investments authorized by this paragraph, and that at the time of purchase, no more than five percent of the investment portfolio shall be invested in the securities of a single issuer.
- Repurchase agreements whose underlying collateral consists of the investments in obligations of the United States Government, its

agencies and instrumentalities, if the political subdivision takes delivery of the collateral either directly or through an authorized custodian. Repurchase agreements do not include reverse agreements.

- An open-end management investment company registered with the Federal Securities and Exchange Commission under the Federal Investment Company Act of 1940, 15 U.S.C. Section 80(a), and operated in accordance with 17 C.F.R. Section 270.2a-7 (more commonly referred to as "constant dollar money market funds").
- A joint investment trust organized pursuant to Chapter 2E, Code of Iowa, prior to and existing in good standing on the effective date of this act or a joint investment trust organized pursuant to Chapter 28E, Code of Iowa, after April 28, 1992, provided that the joint investment trust shall either be rated within the two highest classifications by at least one of the standard rating services approved by the Superintendent of Banking by rule adopted pursuant to Chapter 17A, Code of Iowa, and operated in accordance with 17 C.F.R. Section 270.2A-7, or be registered with the Federal Securities and Exchange Commission under the Federal Investment Company Act of 1940, 15 U.S.C. Section 80(a), and operated in accordance with 17 C.F.R. Section 270.2a-7. The manager or investment advisor of the joint investment trust shall be registered with the Federal Securities and Exchange Commission under the Investment Advisor Act of 1940, 15 U.S.C. Section 80(b).
- Warrants or improvement certificates of a levee or drainage district.

The City Treasurer is not required to invest in all the investment options authorized in this policy. Selection will be based on cash flow characteristics, exposure to market risk, rate of return, the technical ability of the staff responsible for administering the program, and the availability of time and tools for staff to engage in conservative, but effective, management.

11.0 PROHIBITED INVESTMENTS AND INVESTMENT PRACTICES

Assets of the City shall not be invested in the following, according to Code of Iowa 12B.10 (4) and 12B.10 (5):

- Futures and options contracts
- Reverse repurchase agreements

Assets of the City shall not be invested pursuant to the following investment practices:

- Trading of securities strictly for speculation or the realization of short-term trading gains.
- A contract providing for the compensation of an agent or fiduciary based upon the performance of the invested assets.
- If a fiduciary or other third party with custody of public investment transaction records of the City fails to produce records within a reasonable

time, when requested by the City, the City shall make no new investments with or through the fiduciary or third party and shall not renew maturing investments with or through the fiduciary or third party.

12.0 MASTER REPURCHASE AGREEMENTS

A repurchase agreement is a contractual transaction agreement between an investor and an issuing financial institution. The investor exchanges cash for temporary ownership or control of collateral securities with an agreement between the parties that on a future date, the financial institution will repurchase the securities. A signed master repurchase agreement shall be on file with the financial institution with which repurchase transactions are made.

The master repurchase agreement must include the following provisions:

- The underlying collateral shall be limited to the United States Government, agency and instrumentalities.
- Collateral shall be marked to market daily by the custodian and shall be maintained at a value equal to or greater than the cash investment.
- At the time of purchase, the market value of the collateral shall represent 102% of the cash investment.
- An authorized third party custodian or safekeeping agent shall hold all securities purchased under a repurchase agreement.
- A seller of repurchase securities shall not be entitled or authorized to substitute collateral, except as authorized by the City Treasurer.
- Retail repurchase agreements and reverse agreements shall not be authorized for purchase.

13.0 INVESTMENT POOLS

Government sponsored investment pools are sources for short-term cash management. A thorough investigation of the pool is required prior to investing, and on a continual basis. Before investing in these pools, the following issues must be reviewed:

- The pool must meet the requirements of Code of Iowa 12.B10 (5) (a).
- The pool must provide a written statement of policy and objectives.
- A questionnaire should be developed that will address the following general topics:
    - A description of eligible investment securities, and a written statement of investment policy and objectives.
    - A description of interest calculations and how it is distributed, and how gains and losses are treated.
    - A description of how the securities are safeguarded (including the settlement processes), and how often the securities are priced and the program audited.

    - A description of who may invest in the program, how often, what size deposit and withdrawal are allowed.
    - A schedule for receiving statements and portfolio listings.
    - A description of how reserves, retained earnings, etc. are utilized by the pool.
    - A model of the fee schedule, and when and how it is assessed.
    - A description of eligibility and/or acceptance of bond proceeds.
- The pool must contain only the types of investment allowed by this policy.

14.0 SAFEKEEPING AND CUSTODY

14.1 Delivery vs. Payment

All trades of marketable securities, where applicable, will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible financial institution prior to the release of funds. Securities will be held by a third party custodian as evidenced by safekeeping receipts.

14.2 Bonding

City investment officials shall be bonded to protect loss of public funds against possible embezzlement and/or malfeasance.

14.3 Internal Controls

The City Treasurer is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the City of Ames are protected from loss, theft, or misuse.

The internal controls shall address the following points:

- Control of collusion
- Separation of transaction authority from accounting and recordkeeping
- Custodial safekeeping
- Delivery versus payment
- Clear delegation of authority
- Confirmation of transactions for investments and wire transfers

Review of compliance with the internal policy and related procedures shall be a part of the annual audit process conducted by the City's independent auditors.

15.0 COLLATERAL/SECURITY FOR DEPOSIT OF PUBLIC FUNDS

15.1 Commercial Banks and Savings and Loans

The City shall make deposits only with commercial banks and savings and loans that comply with Section 12C of the Code of Iowa, "Deposit of Public Funds", and Section 12C, Subsection 22 of the Code of Iowa, "Required Collateral."

15.2 Credit Unions

Before a deposit of public funds is made with a credit union in excess of the amount federally insured, the public officer shall obtain security for the deposit by one or more of the following:

- Surety bond of a surety company approved by the United States Treasury and authorized to do business in the State of Iowa and shall be an amount equal to the public funds on deposit at any time.
- Deposit, maintain, pledge, and assign for the benefit of the public entity. The securities shall be approved by the public officer, the market value of which is not less than 110% of the total deposits of the funds on deposit for that public entity in the credit union. These securities shall be deposited with the Federal Reserve Bank, the Federal Home Loan Bank of Des Moines, Iowa, or the U. S. Central Credit Union.
- Irrevocable letter of credit issued by the National Credit Union Administration naming the City of Ames as beneficiary.
- Withdrawal or exchange of the securities may be done only with the written approval of the appropriate public officer.

16.0 DIVERSIFICATION

The purpose of diversification is to reduce overall portfolio risk while attaining market rates of return and to enable the City of Ames to meet all anticipated cash requirements.

The investments shall be diversified by:

- Limiting investments to avoid over-concentration in securities of a specific issuer (excluding treasury bills).
- Limiting investment in securities that have higher credit risks.
- Limiting certificates of deposit to the amount approved by City Council for each financial institution in accordance with the <u>Code of Iowa</u>.
- Investing in securities with varying maturities.
- Investing a minimum of 5% of the total portfolio in highly marketable short-term treasuries, checking accounts with interest, government pooled account, or a combination of all three.

17.0 MAXIMUM MATURITIES

To the extent possible, the City of Ames will attempt to match its investments with anticipated cash flow requirements.

17.1 <u>Operating Funds</u>

Operating funds are those funds that can be reasonably expended during a current budget year or within fifteen months of receipt. These funds may only be invested in instruments that mature within three hundred ninety-seven (397) days or less. Operating funds must be identified and distinguished from all other funds available for investment. (Section 12B.10A, Code of Iowa)

17.2 Non-Operating Funds
Reserve funds for debt service, and funds being accumulated for capital improvements on a pay-as-you-go basis that are not required for operations may be invested for longer than three hundred ninety-seven (397) days (Section 12B.10A(3), Code of Iowa). These maturities shall coincide as nearly as possible with the anticipated need. The City of Ames will keep these investments for a duration not to exceed seven (7) years.

18.0 REPORTING

18.1 Methods
The City Treasurer shall prepare an investment report quarterly and present to the City Council within 45 days of each quarters end. This report will include the following:

- List of individual securities held at the end of the reporting period further broken down by issuer, purchase date, maturity date, coupon rate, par value, market value, book value, and yield to maturity.
- A report summarizing the portfolio by type, the percentage of the total portfolio which each type of investment represents, par value, market value, book value, term, days to maturity, year-to-date earnings and effective rate of return.

18.2 Performance Standards
The market value is calculated monthly and reported to the City Council quarterly. The portfolio is benchmarked to the applicable treasuries constant maturities rate as reported by the Federal Reserve.

19.0 POLICY CONSIDERATION

19.1 Exemption
Any investment currently held that does not meet the guidelines of this policy shall be exempted from the requirements of this policy as long as it was in compliance with State of Iowa law and the City's investment policy in effect at the time of purchase. At maturity or liquidation, such monies shall be reinvested only as provided by this policy.

19.2 Amendments
This policy shall be reviewed annually to ensure consistency to overall objectives of safety, liquidity, yield, compliance to current law, and economic trends.

19.3 This investment policy is required by Code of Iowa, Section 12B.10B and approved by City Council.

APPENDIX

ACCRUED INTEREST: The accumulated interest payable on a security since the last interest payment made by the issuer.

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

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

ASKED: The price at which 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.

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

BENCHMARK: A comparative base for measuring the performance or risk tolerance of the investment portfolio. A benchmark should represent a close correlation to the level of risk and the average duration of the portfolio's investment.

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

BOOK ENTRY: An electronic system of accountability, custody, transfer, and settlement of securities. Book-entry systems allow rapid and accurate transfers of securities with simultaneous cash settlement.

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

BROKER: A broker brings buyers and sellers together for a commission.

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

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

CERTIFICATE OF DEPOSIT (CD): A time deposit with a specific maturity evidenced by a certificate. Large-denomination CDs are typically negotiable.

CERTIFICATE OF DEPOSIT ACCOUNT REGISTRY SERVICE (CDARS): A program with an approved depository that removes the need for collateral by providing full FDIC insurance for certificates of deposit.

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.

COLLATERLIZED MORTGAGE OBLIGATION (CMO): Mortgage backed bond that separates mortgage pools into different maturity classes called traunches. CMO's are issued by Federal National Mortgage Corp. and Federal National Mortgage Association and are usually backed with a government guarantee and have an AAA bond rating. Planned Amortization Class CMOs (PAC) have stable prepayment schedules that do not react unfavorably in wide market swings.

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

COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR): The official annual report for the entity. It includes five combined 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 QUALITY: The measurement of the financial strength of a bond issuer. This measurement helps an investor to understand an issuer's ability to make timely interest payments and repay the loan principal upon maturity. Generally, the higher the credit quality of a bond issuer, the lower the interest rate paid by the issuer because the risk of default is lower. Credit quality ratings are provided by nationally recognized rating agencies.

CREDIT RISK: The risk to an investor that an issuer will default in the payment of interest and/or principal on a security.

CURRENT YIELD (CURRENT RETURN): A yield calculation determined by dividing the annual interest received on a security by the current market price of that security.

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. 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.

DERIVATIVES: (1) Financial instruments whose return profile is linked to, or derived from, the movement of one or more underlying index or security, and may include a leveraging factor; or (2) financial contracts based upon notional amounts whose value is derived from an underlying index or security (interest rates, foreign exchange rates, equities or commodities).

DISCOUNT: The difference between the cost price of a security and its 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.

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

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

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

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

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

FEDERAL 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): Government sponsored wholesale banks (currently 12 regional banks) which lend funds and provide correspondent banking services to member commercial banks, thrift institutions, credit unions and insurance companies. The mission of the FHLBS is to liquefy the housing related assets of its members who must purchase stock in their district bank.

FEDERAL HOME LOAN MORTGAGE CORPORATION (FHLMC): Established to help maintain the availability of mortgage credit for residential housing. Participation is in the conventional loan market.

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 (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’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.

FIDUCIARY: Person, company, or association holding assets in trust of a beneficiary.

FUTURES CONTRACT: Agreement to buy or sell a specific amount of a commodity or financial instrument at a particular price on a stipulated future date.

GOVERNMENT NATIONAL MORTGAGE ASSOCIATION (GNMA OR GINNIE MAE): Securities influencing the volume of bank credit 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 the FHA, VA or FmHA mortgages. The term “pass-through” is often used to describe Ginnie Maes.

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

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

INVESTMENT POLICY: A concise and clear statement of the objectives and parameters formulated by an investor or investment manager for a portfolio of investment securities.

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.

MARK-TO-MARKET: The process whereby the book value or collateral value of a security is adjusted to reflect 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.

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 Asked and 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.

OPTION: Right to buy or sell property that is granted in exchange for an agreed upon sum. If the right is not exercised after a specified period, the option expires and the option buyer forfeits the money.

PORTFOLIO: Collection of securities held by an investor.

PRIMARY DEALER: A group of government securities dealers who 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. 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 custody 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.

REINVESTMENT RISK: The risk that a fixed-income investor will be unable to reinvest income proceeds from a security holding at the same rate of return currently generated by that holding.

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.

SPECULATION: Assumption of risk in anticipation of gain but recognizing a higher than average possibility of loss.

STRUCTURED NOTES: Notes issued by Government Sponsored Enterprises (FHLB, FNMA, 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.

SWAP: Trading one asset for another.

TOTAL RETURN: The sum of all investment income plus changes in the capital value of the portfolio. For mutual funds, return on an investment is composed of share price appreciation plus any realized dividends or capital gains. This is calculated by taking the following components during a certain time period.

(Price Appreciation) + (Dividends Paid) + (Capital Gains) = Total Return

TREASURY BILLS: 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 BONDS: Long-term coupon-bearing U. S. Treasury securities issued as direct obligations of the U. S. Government and having initial maturities of more than ten years.

TREASURY NOTES: Medium-term coupon-bearing U. S. Treasury securities issued as direct obligations of the U. S. Government and having initial maturities from two 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.

VOLATILITY: A degree of fluctuation in the price and valuation of securities.

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

WHEN ISSUED (WI): A conditional transaction in which an authorized new security has not been issued. All "when issued" transactions are settled when the actual security is issued.

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 for 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.

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

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

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

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

BROKER/DEALER QUESTIONNAIRE AND CERTIFICATION

1. Name of Firm ____

2. Local Address

   ____
   ____
   ____
   ____

   National Headquarters

   ____
   ____
   ____
   ____

3. Local Telephone Number(s), Toll-Free Number(s)

   ______________________________ ______________________________

4. Primary Representative/Manager/Partner-in-Charge

   Name_________________________ Name_________________________

   Title _________________________ Title_________________________

5. Is the firm a primary or regional dealer in U. S. Government Securities, as designated by the Federal Reserve of New York, qualifying under S.E.C. Uniform Net Capital Rule 15c3-1?

   Primary _____ Yes _____ No Regional _____ Yes _____ No

   If yes, how long has the firm been a primary dealer? ______ years
   If yes, how long has the firm been a regional dealer? ______ years

6. Is the firm a commercial bank or an NASD member affiliate of a bank chartered under the laws of one of the United States?

   _____ Yes Chartered under laws of the state of __________________.
   _____ No

   If yes, are the bank customers' deposits insured by the Federal Deposit Insurance Corporation?
   _____ Yes _____ No

7. Place an “X” by each regulatory agency that your firm is examined by and/or subject to its rules and regulations.

    _____FDIC _____SEC _____NYSE _____Comptroller of Currency
    _____Federal Reserve System
    _____Other (Example: State Regulatory Agency) Multistate firms please note: It is not necessary to include regulatory agencies which do not have jurisdiction over your firm’s activities in Local Government Jurisdiction.

8. Is the firm licensed to sell securities in the state of Iowa?

    _____ Yes _____ No

9. Is/Are the person(s) designated to service the City’s account licensed to sell securities in the state of Iowa?

    _____ Yes _____ No

10. Is the firm a member of the Federal Reserve System? _____ Yes _____ No

11. What was the firm’s approximate total retail volume in U. S. Treasury and Agency securities last year?
    Firm wide $ ____________________ # of Transactions _______________

    Local Office $__________________ # of Transactions _______________

12. Identify personnel who will be trading with or quoting prices of securities to our government.

    Name____________________________ Title____________________________

    Name____________________________ Title____________________________

13. Fully disclose the method in which you would be compensated for your services.

14. Please identify the firm’s most directly comparable public sector clients in our geographical area.

    Entity_____________________________ Contact Person___________________
    Telephone #______________________ Client since_______________________

    Entity_____________________________ Contact Person __________________
    Telephone #______________________ Client since_______________________

15. Place an “X” in the block next to each of the instruments set forth below in which you make an active market (both buy and sell).

_____T-Bills _____T Notes/Bonds
_____BA _____Commercial Paper
_____Bank CDs _____S & L CDs
_____GNMAs _____FHLMCs
_____Other Federal Agencies (Please Specify)____________________________
_____Instrumentalities (Please Specify)__________________________________

16. Does your firm specialize in any of the instruments listed above? If so, please specify which ones.

____
____
____

17. Have any of your public sector clients ever reported to the firm, its officers or employees, that they sustained a loss (in a single year) exceeding ten percent of original purchase price on any individual security purchased through the firm?

Explain____
____
____

18. Has the firm ever been subject to a regulatory or state/federal agency investigation for alleged improper, fraudulent, disreputable, or unfair activities related to the sale of securities?

Explain____
____
____
____

19. Who audits the fiduciary systems of the firm’s custody and delivery processes?

____

20. Has the firm consistently complied with the Federal Reserve’s Capital Adequacy Standard? _____ Yes _____ No

21. By what factor (1.5x, 2x, etc.) does the firm presently exceed the Capital Adequacy Standard’s measure of risk? ____

22. Has the firm’s capital position ever fallen short of the Capital Adequacy Standard? _____ Yes _____ No

23. What portfolio information do you require from your clients?

____
____
____
____

24. What reports, confirmations, documents and audit trail will we receive?
____
____
____
____

25. Approximately how many and what percentage of the firm's transactions failed last month?
_____ # transactions _______%

Last year?
_____ # transactions _______%

26. Describe the precautions taken by the firm to protect the interest of the public when dealing with governmental agencies as investors.
____
____
____
____
____

27. Please supply the following:

A. The firm's most recent audited annual financial report and most recent quarterly report.

B. Proof of the firm's designation by the Federal Reserve Bank of New York as a "primary securities dealer" <u>OR</u> Proof of FDIC coverage.

C. Proof of individual's (assigned to service the City's account) State of Iowa securities sales license.

D. Proof of the firm's State of Iowa securities sales license.

<u>CERTIFICATION</u>

I hereby certify that sales personnel assigned to the City of Ames, Iowa account have received and read a copy of the City's Investment Policy. For each transaction, we pledge to exercise due diligence in disclosing all information necessary for each party to agree to the details of the transaction. When recommending a transaction, we will have reasonable grounds for believing the transaction is suitable based upon information available from the issuer and based upon the facts disclosed by the City of Ames, Iowa, or otherwise known about such customer. We have implemented investment procedures and a system of controls designed to preclude imprudent investment activities arising out of transactions conducted between our firm and the City of Ames, Iowa. I attest to the accuracy of our responses to the questionnaire.

Signed ______________________________ Date___________________________

Title ________________________________