

**INVESTMENTS
(Chapter 7)**

TABLE OF CONTENTS

Introduction	122
Cash Management	122
Fiduciary Responsibilities of Board Members	122
The Investment Policy.....	123
Investment Restrictions	125
Written Investment Procedures.....	125
Resources	127

INTRODUCTION

Investing is an important part of using district funds efficiently, and maximizing resources. Even small districts with limited expertise can take advantage of investment opportunities that have been created specifically for small public organizations.

Oregon Revised Statute, Chapter 294, "Municipal Financial Administration," provides the investment authorization for special districts. If this chapter does not specifically authorize an investment, then districts are forbidden from making that type of investment. In addition, no district may invest money unless its board has authorized the investment.

Normally, the district board appoints a staff investment officer, such as the manager or chief financial officer, and approves the investment policy. The adoption of an investment policy provides authorization and guidelines for the types of investments that will be permitted. The policy should be put in writing and state that it complies with applicable state statutes. The policy should also set guidelines for diversification, liquidity, and maturity of investments.

The Oregon Short Term Fund Board, "strongly recommends that local governments with limited amounts of money to invest, or with limited time and resources to devote to their investment, concentrate on making sure that their investments are safe (there is no appreciable risk that the investment will fail) and liquid (the investment can be easily converted to cash)." The lowest priority of objectives should be attached to maximizing the rate of return.

CASH MANAGEMENT

Investing is part of a cash management program. The objective of cash management is to have sufficient liquidity to pay obligations when they are due while minimizing borrowing expenses and maximizing investment revenues from surplus funds.

Surplus funds are monies, which temporarily exceed cash flow requirements. Typically these funds are monies reserved for capital expenditures, fall tax turnovers (when a large percentage of annual revenue is received in a short period of time and will not be disbursed until later in the year), bond sale proceeds, carryover funds from the previous fiscal year (cash on hand), system development charge income, grant proceeds, etc.

Good cash management practices encourage the investment of monies which in turn increases revenue. Reasonable rates of return on investments can be obtained while maintaining security and liquidity. In some cases, investment earnings can even reduce tax rates or user charges.

FIDUCIARY RESPONSIBILITIES OF BOARD MEMBERS

Board members can be held personally liable for certain financial misdeeds of the organization. There are several actions board members should take to protect themselves from exposure to litigation. These include:

- Purchase of appropriate liability insurance coverage for the governing body. *Note: If you do not currently have this coverage, SDIS has coverage options available to members.*
- Put an investment policy in writing.
- Insist on adequate financial reporting from staff.

- Understand the board’s powers, responsibilities, and any legal restrictions.
- Seek expert advice before taking any action in which the board lacks reasonable competence to handle.
- Understand the principals of investment so that the board can manage the investment manager.

THE INVESTMENT POLICY

Since any investment made by a district requires authorization by the board, it is recommended that all districts have an adopted investment policy. A policy is useful regardless of the type of investing a district intends to pursue. The policy should be easily understood by individuals with or without investment expertise.

The Oregon Short Term Fund Board recommends, in its "Local Government Investment Policy Guidelines," creating a written investment policy for several reasons. An investment policy can:

- Increase investment flexibility.
- Reduce investment risk.
- Improve the district board’s understanding of the investment process.
- Allow the district board to deal with the investment policy in a consistent and clear manner.
- Acquaint the investment officer with the investment preferences of their board, and provide the investment officer with rules to avoid misunderstanding and liability.
- Provide written guidance to new or substitute investment officers, who may not be familiar with investment or the district’s past practices, and who might otherwise make inappropriate investments.

Key elements of an investment policy should consist of the following:

- Scope: Identifies funds under the authority of the policy.
- Objectives: (Prioritized)
 - Safety
 - Liquidity
 - Return
- Standards of Care:
 - Prudence (Prudent Person Standard)
 - Ethics and Conflicts of Interest
 - Indemnification for investment decisions
 - Delegation of Authority
 - Internal Controls
 - Separation of investment decisions and recordkeeping
- Safekeeping & Custody:
 - Delivery vs. Payment protocol

- Safekeeping/Custody by 3rd Party
- Authorized Investments: Specific authorized investment types should be listed
- Risk Parameters:
 - Credit Risk:
 - Ratings requirements
 - Exposure limitations
 - Interest Rate Risk:
 - Maximum investment maturity
 - Maximum average maturity
 - Concentration Risk:
 - Diversification requirements
 - Liquidity Risk:
 - Minimum liquidity guidance
 - Maturity buckets
- Transaction Counterparties:
 - Minimum requirements to approve broker/dealers
 - Minimum requirements to approve investment advisers
- Policy Compliance:
 - Reporting requirements:
 - Required data
 - Periodicity of reporting
 - Recipients of reports
 - Guideline violation resolution
- Policy Maintenance
 - Periodic Policy Review

INVESTMENT METHODS AVAILABLE TO SPECIAL DISTRICTS

Oregon law restricts special districts to specific types of investments. The following is a short description of the types of investments that districts can legally utilize.

- US Treasury Obligations: U.S. Treasury and other government obligations that carry the full faith and credit guarantee of the United States for the timely payment of principal and interest.
- US Agency Obligations: Senior debenture obligations of US federal agencies and instrumentalities or U.S. government sponsored enterprises (GSE).
- Oregon Short Term Fund.
- Corporate Indebtedness
 - Commercial paper issued under the authority of section 3(a)2 or 3(a)3 of the Securities Act of 1933.
 - Corporate Bonds
- Repurchase Agreements
- Municipal Debt

- Bankers Acceptances
- Qualified Institution Time Deposits.Savings Accounts/Certificates of Deposit.

A list of investments allowed under ORS 294.040 and 294.810 may be found on the Oregon State Treasury website:

Other Investments

Oregon statutes permit certain other investments and transactions for special purpose funds in limited circumstances. For example, fixed or variable life insurance or annuity contracts, guaranteed investment contracts, and, for deferred compensation funds, share and savings accounts in credit unions and trusts. Seek advice of legal counsel if these investments are contemplated.

INVESTMENT RESTRICTIONS

Oregon law places certain restrictions on local government investing. ORS 294 prohibits local governments from:

- Committing to invest funds more than 14 days in advance of settlement.
- Agreeing to invest funds or sell securities for a fee other than interest.
- Lending securities, unless authorized by an investment policy which has been reviewed by the Short Term Fund Board.
- Paying for securities before the local government or a custodian bank receives physical delivery of the securities.
- Delivering securities to a purchaser prior to receiving payment in full.

In addition, investments may not have a maturity in excess of eighteen months unless the governing body adopts a written investment policy, and that policy is reviewed by the Oregon Short Term Fund Board. The investment policy must include guidelines concerning maximum investment maturity dates and require readoption, not less than annually. This eighteen month restriction does not apply to money which the local government is specifically authorized by state law to hold for more than one year, if the money is invested in securities which mature when the money is expected to be needed and to certain reserves for bonds and construction projects.

WRITTEN INVESTMENT PROCUDURES

Instituting written investment procedures offers several benefits apart from an investment policy. Written procedures outline the process for making investment decisions, detail the activities of the investment staff, and specify how investment decisions are to be carried out. An investment policy should succinctly state the entity's investment objectives, outline the risk tolerances of the governing body, and delegate authority to investment personnel. In contrast, an investment procedure should formalize the investment process and put the investment policy into action.

Well-written investment procedures will answer the following questions:

- Who is authorized to initiate investment transactions?
- Who is authorized to approve investment transactions?
- Who is authorized to initiate fund transfers or wire transactions?
- Who will make investment bookkeeping and accounting entries?
- Who are the approved broker/dealers and financial institutions for transacting business on a day-to-day basis?
- Who is the safekeeping agent and what are the delivery instructions?

When developing written procedures, it is helpful to think through the entire investment process from beginning to end, and then document the activities that take place. Investment procedures should begin with a review of the daily cash position and include a review of maturing investments and incoming payments.

Next, the procedures should detail how investment decisions will be made. How will cash flow needs be determined? What are current and expected interest rates? What other investments are in your entity's portfolio? Written procedures should outline or detail how investment transactions will be handled.

To help ensure compliance with the investment policy and adherence to internal controls, the items listed below should be included in the procedure:

- Governing statutes, regulations, ordinances, resolutions, and policies.
- Duties of personnel.
- Limitations of employee authority.
- Flowchart of transaction initiation and execution.
- Lists of authorized broker/dealers and financial institutions who may be called for competitive quotes on securities.
- List of relevant bank account numbers, safekeeping, and delivery instructions.
- Descriptions of relevant cycles and functions, including review and approval processes.
- Timelines for report preparation and report distribution lists.
- Methodologies and formulas for allocations, distributions, and other calculations.
- Samples of all forms and reports.
- Descriptions of back-up and disaster recovery procedures.
- Implementation dates and dates of revisions.

Some investment procedure manuals go beyond the daily routine and outline what activities should take place on a monthly, quarterly, periodic, and annual basis. For example, the

procedure manual might include information on how broker/dealers and financial institutions are selected, how often those institutions are reviewed for creditworthiness, and who is responsible for this review. Written procedures should be reviewed and updated annually.

RESOURCES

County and Municipal Financial Administration (ORS 294):

https://www.oregonlegislature.gov/bills_laws/ors/ors294.html

Local Government Investment Pool:

<http://www.oregon.gov/treasury/divisions/finance/localgov/pages/lqip%20resources.aspx>

Oregon State Treasury Finance Division Home Page:

<http://www.oregon.gov/treasury/Divisions/Finance/Pages/default.aspx>

Public Funds Collateralization Program:

<http://www.oregon.gov/treasury/Divisions/Finance/FinancialInstitutions/Pages/PFCP%20for%20Banks.aspx>

SDAO Reference Library/Accounting: <http://www.sdao.com/S4/MemberHome.aspx>