RESOLUTION NO. 2017-1

A RESOLUTION OF THE TOWN COUNCIL OF THE TOWN OF FAIRVIEW, TEXAS, REVIEWING AND APPROVING THE WRITTEN INVESTMENT POLICY REGARDING FUNDS FOR THE TOWN OF FAIRVIEW; AND PROVIDING AN EFFECTIVE DATE.

WHEREAS, Section 2256.005(e) of the Texas Government Code requires the governing body of an investing entity to adopt a written investment policy regarding the investment of its funds and funds under its control and to review said written investment policy on an annual basis; and

WHEREAS, on January 5, 2016, the Town Council approved and adopted a written Investment Policy for the Town of Fairview regarding investment of public funds; and

WHEREAS, The Town Council desires to revise the Investment Policy in order to reflect changes in the Public Funds Investment Act (PFIA), as well as incorporate needed administrative and procedural modifications which have occurred over this past year; and

WHEREAS, Government Code Chapter Sec. 2256.008 pertaining to investment training has changed training requirements from 10 to 8 hours every two years for municipality Investment officers that have completed 12 months of assumed duties; and

WHEREAS, the Town's Authorized Investments have been changed to reflect the wording from the Government Code Chapter Sec.2256.009 Obligations of, or Guaranteed by Governmental Entities; Sec. 2256.010 Certificates of Deposit and Share Certificates; Sec. 2256.011 Repurchase Agreements; Sec. 2256.0115 Securities Lending Program; Sec. 2256.012 Bankers Acceptances; Sec. 2256.013 Commercial Paper; Sec. 2256.14 Mutual Funds; Sec. 2256.015 Guaranteed Investment; Sec. 2256.016 Investment Pools; and

WHEREAS, the Town's Prohibited Investments have been changed to reflect the wording from the Government Code Chapter Sec.2256.009(b) with additions of; Bonds issued, assumed, or guaranteed by the State of Israel; A fully collateralized repurchase agreement; A securities lending program; and A bankers' acceptance; and

WHEREAS, the Town Council has been presented the existing and duly approved Public Funds Investment Policy which contains investment strategies, a copy of which is attached hereto as Exhibit "A" and incorporated herein by reference; and,

WHEREAS, the Town Council has reviewed the Public Funds Investment Policy attached hereto as Exhibit "A" and the investment strategies contained therein and funds that it is consistent with prudent fiscal policy.

NOW, THEREFORE, BE IT RESOLVED BY THE TOWN COUNCIL OF THE TOWN OF FAIRVIEW:

SECTION 1: The Town Council of the Town of Fairview, Texas has reviewed the Public Funds Investment Policy attached hereto as Exhibit "A" and the investment strategies contained herein.

SECTION 2: The Public Funds Investment Policy as contained in Exhibit "A" attached hereto shall be the official policy of the Town of Fairview regarding investment of public funds, unless amended by the Town Council in the future. All previous policies adopted by the Council are hereby rescinded.

SECTION 3: This Resolution shall take effect immediately upon its passage.

PASSED AND APPROVED by the Town Council of the Town of Fairview, Texas this the 3rd day of January, 2017.

Darion Culbertson, Mayor
Town of Fairview, Texas

ATTEST:

Elizabeth Cappon, Town Secretary
Town of Fairview, Texas

TOWN OF FAIRVIEW

APPROVED AS TO FORM:

Clark McCoy, Town Attorney

Exhibit "A"

TOWN OF FAIRVIEW
INVESTMENT POLICY

I. PURPOSE

It is the objective of the Town of Fairview to invest public funds in a manner which will provide maximum security and the best commensurate yield while meeting the daily cash flow demands of the Town and conforming to all federal, state and local statutes, rules, and regulations governing the investment of public funds. This Investment Policy serves to satisfy the statutory requirements of defining and adopting a formal investment policy. The Investment Policy and investment strategies shall be reviewed annually by the Investment Committee and Town Council who will formally approve any modifications. This Investment Policy, as approved, is in compliance with the provisions of the Public Funds Investment Act of Texas Government Code Chapter 2256 as amended by H.B. 1184 and 870.

II. SCOPE

A. This Investment Policy applies to the investment activities of the Town of Fairview, Texas. The specific funds cited hereafter, shall be excluded from this Investment Policy. All financial assets of all funds, including the General Fund and any other accounts of the Town not specifically excluded in these policy guidelines are included. These funds are accounted for in the Town's Comprehensive Annual Financial Report (CAFR). These funds, as well as funds that may be created from time-to-time, shall be administered in accordance with the provisions of this Policy. All funds will be pooled for investment purposes except for those listed under IIC.

In addition to this Policy, the investment of bond proceeds and other bond funds (including debt service and reserve funds) shall be governed and controlled by their governing ordinance and by the provisions of the Tax Reform Act of 1986, including all regulations and rulings promulgated there under applicable to the issuance of tax-exempt obligations.

B. Funds covered by this Policy and managed as a pooled fund group:

1. General Fund – used to account for resources traditionally associated with government, which are not required to be accounted for in another fund.

2. Special Revenue Fund – used to account for the proceeds from specific revenue sources which are restricted to expenditures for specific purposes.

3. Debt Service Fund – used to account for resources to be used for the payment of principal, interest and related costs on general obligation debt and capital leases.

4. Capital Project Funds – used to account for resources to enable the acquisition or construction of major capital facilities which are not financed by enterprise funds, internal service funds or trust funds.

5. Enterprise Funds – used to account for operations that are financed and operated in a manner similar to private business enterprises.

6. Trust & Agency Funds – used to account for assets held by the Town in a trustee capacity or as an agent for individuals, private organizations, other governments and/or other funds.

7. Bond Reserve Funds – funds set at prescribed levels by certain bond ordinances to pay principal and/or interest if required to prevent default.

8. Other funds as they become available for investment by the Town, such as (but not limited to) resources associated with Public Improvement Districts or Tax Increment Financing zones, unless specifically excluded herein.

C. Funds covered by this Policy and managed as separately invested assets:

1. Bond Funds – funds established with the proceeds from specific bond issues when it is determined that segregating these funds from the pooled funds' portfolio will result in maximum interest retention under the provisions of the Tax Reform Act of 1986.

2. Endowment Funds – funds given to the Town with the instructions that the principal is to remain intact, unless otherwise agreed to, and the income generated by the investments will be used for specified purposes.

3. Trust or Escrowed Funds – funds held outside the Town by a trust or escrow agent but belonging to the Town.

D. This Policy shall not govern funds, which are managed under separate investment programs in accordance with the Texas Government Code Section 2256.004. Such programs currently include all funds related to employee retirement programs, other funds established by the Town for deferred employee compensation, and certain private donations. The Town shall and will maintain responsibility for these funds to the extent required by federal and state law and donor stipulations. This Policy also does not apply to monies held in escrow to retire bonds which are subject to defeasance requirements stated under their respective bond ordinances.

III. INVESTMENT OBJECTIVES & STRATEGIES

It is the policy of the Town that, giving due regard to the safety and risk of investments, all available funds shall be invested in conformance with state and federal regulations, applicable bond ordinance requirements, adopted Investment Policy and investment strategies.

In accordance with the Public Funds Investment Act, the following prioritized objectives (in order of importance) in accordance with the Texas Government Code Section 2256.005(d) apply for each of the Town's investment strategies.

A. *Suitability* – Understanding the suitability of the investment to the financial requirements of the Town is important. Any investment eligible in the Investment Policy is suitable for all Town funds.

B. *Safety* – Safety of principal is the foremost objective of the investment program. All investments will be in high quality securities with no perceived default risk. Investments of the Town shall be undertaken in a manner that seeks the preservation of capital in the overall portfolio. Each investment transaction shall be conducted in a manner to control the risk of capital loss by investing in securities or other investments of high quality. The objective will be to mitigate credit and interest risk.

- Credit Risk and Concentration of Credit Risk – The Town will minimize credit risk, the risk of loss due to the failure of the issuer or backer of the investment, and concentration of credit risk, the risk of loss attributed to the magnitude of investment in a single issuer by:
    - Limiting investments to the safest types of investments;
    - Pre-qualifying the financial institutions and brokers/dealers with which the Town will do business with;
    - Diversifying the investment portfolio so that potential losses on individual issuers will be minimized; and
    - Monitoring credit rating changes in investments acquired with public funds and the liquidation of such investments consistent with the provision of Section 2256.021.

- Interest Rate Risk – The Town will minimize the risk that the market value of investments in the portfolio will fall due to changes in general interest rates by limiting the maximum weighted average maturity of the investment portfolio to 730 days. The Town will, in addition:
  - Structure the investment portfolio so that investments mature to meet cash requirements for ongoing operations, thereby avoiding the need to liquidate investments prior to maturity; and
  - Diversify maturities and staggering purchase dates to minimize the impact of market movements over time.

C. *Liquidity* – The Town's investment portfolio will remain sufficiently liquid to meet operating requirements that might be reasonably anticipated. Liquidity shall be achieved by matching investment maturities with forecasted cash flow requirements and by investing in securities with active secondary markets. Short-term investment pools and money market mutual funds provide daily liquidity and may be utilized as a competitive investment alternative to fixed income instruments.

D. *Marketability* – Securities with active and efficient secondary markets are necessary in the event of an unanticipated cash requirement. Historical market "spreads" between the bid and offer prices of a particular security type of less than a quarter of a percentage point shall define an efficient secondary market.

E. *Diversification* – Investment maturities shall be staggered to provide cash flow based on the anticipated needs by the Town. Diversifying the appropriate maturity structure will reduce market cycle risk.

F. *Yield* – Attaining a competitive market yield, commensurate with the Town's investment risk constraints and the cash flow characteristics of the portfolio, is the desired objective. The goal of the Town's investment portfolio is to regularly meet or exceed the average rate of return on U.S. Treasury Bills at maturity level comparable to the portfolio's weighted average to maturity in days. The yield of an equally weighted, rolling six-month U.S. Treasury Bill portfolio shall be the minimum yield objective or "benchmark". Six-month U.S. Treasury Bill information is derived from the Federal Reserve Statistical Release H.15 for constant maturities. A secondary objective will be to obtain a yield equal to or in excess of a local government investment pool or money market mutual fund.

The first measure of success in this area will be the attainment of enough income to offset inflationary increases. Although steps will be taken to obtain this goal, the

Town's staff will follow the "Prudent Person" statement relating to the standard of care that must be exercised when investing public funds as expressed in the Texas Government Code Section 2256.006(a-b). The Investment Officer(s) shall avoid any transactions that might impair public confidence in the Town's ability to govern effectively. The governing body recognizes that in adequately diversifying the maturity structure within the portfolio to meet the Town's expenditure needs, occasional measured unrealized losses due to market volatility and rising interest rates are inevitable, and must be considered within the context of the overall portfolio's investment return. The prudence of the investment decisions shall be measured in accordance with the tests set forth in the Texas Government Code Section 2256.006(b).

IV. INVESTMENT STRATEGY FOR SPECIFIED FUND GROUPS

In order to better diversify, maximize interest earnings and otherwise meet stated objectives, fund groups may be combined into one or more internal investment pools. Although fund monies may be combined into a single asset portfolio, proportional fund ownership will be accounted for separately. One of the fund's primary objectives is to insure that anticipated cash flows are matched with investment maturities. Both short and longer-term maturities are laddered to meet general operating, capital project and debt service expenditures, based on known and projected cash flows.

Another primary objective of the fund is the preservation and safety of principal by insuring that all securities are of a sufficiently high quality and duration so as to limit exposure to credit and market risks. The portfolio should therefore experience minimal volatility during varying economic cycles. Securities of all types are purchased with the intention of holding until maturity.

Other objectives include maintaining liquidity, including the ability to reasonably meet unanticipated needs by purchasing securities with an active secondary/resale market. Diversification is maintained in order to minimize possible credit risk in a specific security type.

The Town maintains separate portfolios for some individual funds or groups of funds (as listed under Section II) that are managed in accordance with the terms of this Policy and by the corresponding investment strategies listed below.

A. *Investment Pool Strategy* – The Town's Investment Pool is an aggregation of the majority of Town funds which includes tax receipts, enterprise fund revenues, fine and fee revenues, as well as some, but not necessarily all, bond proceeds, grants, gifts and endowments. This portfolio is maintained to meet anticipated daily cash needs for the Town's operations, capital projects and debt service. The objectives of this portfolio are to:

1. Ensure safety of principal by investing in only high quality securities for which a strong secondary market exists.

2. Ensure that anticipated cash flow needs are matched with adequate investment liquidity.

3. Limit market and credit risk through diversification.

4. Attain the best feasible yield commensurate with the objectives and restrictions set forth in this Policy by actively managing the portfolio to meet or exceed the six month moving average yield on a six month U.S. Treasury Bill as derived from the Federal Reserve Statistical Release H.15 for constant maturities.

B. *Bond Funds Strategy* – Occasionally, separate non-pooled portfolios are established with the proceeds from the bond sales in order to maximize earnings within the constraints of arbitrage regulations. The objectives of the portfolios are to:

1. Ensure safety of principal by investing in only high quality securities for which a strong secondary market exists.

2. Ensure that anticipated cash flow needs are matched with adequate investment liquidity.

3. Limit market and credit risk through diversification.

4. Attain the best feasible yield commensurate with the objectives and restrictions set forth in this Policy and the bond ordinance by actively managing the portfolio to meet or exceed the bond yield.

C. *Endowment Fund Strategy* – Funds received as gifts to the Town with instructions that the income generated by the investment of said funds be used for specified purposes are invested as separate non-pooled portfolios in order to maximize return. The objectives of the portfolios are to:

1. Ensure safety of principal by investing in only high quality securities for which a strong secondary market exists.

2. Ensure that anticipated cash flow needs are matched with adequate investment liquidity.

3. Limit market and credit risk through diversification.

4. Attain the best feasible yield commensurate with the objectives and restrictions set forth in this Policy.

D. *Trust or Escrowed Funds Strategy* – Funds that are held outside the Town by a trust or escrow agent but belonging to the Town are governed by their respective trust or escrow agreement and are subject to the provisions of this Policy. This objectives of the portfolios are to:

1. Ensure safety of principal by investing in only high quality securities for which a strong secondary market exists.

2. Ensure that anticipated cash flow needs are matched with adequate investment liquidity.

3. Limit market and credit risk through diversification.

4. Attain the best feasible yield commensurate with the objectives and restrictions set forth in this Policy and the trust/escrow agreement.

V. INVESTMENT COMMITTEE

Members – The Investment Committee will consist of the Town Manager, Chief Financial Officer, Town Treasurer, Assistant to Town Manager and the Accounting Manager are appointed to the committee annually upon the approval of this policy and the Town's investment advisor (if applicable). If applicable, the investment advisor is a non-voting member. When needed, the Town Attorney will act as a legal advisor to the Investment Committee.

Scope – The Investment Committee shall meet at least annually, but may meet as often as needed to determine general strategies, investment guidelines and to monitor results. Included in its deliberations will be such topics as: economic outlook, portfolio diversification, maturity structure, potential risk to the Town's funds, authorized broker/dealers (if applicable) and depository institutions, as well as the target rate of return on the investment portfolio.

Procedures – The Investment Committee shall provide meeting information to all members. Any members of the Investment Committee may request a special meeting. The Investment Committee shall establish its own rules of procedures.

VI. RESPONSIBILITY AND STANDARD OF CARE

A. *Delegation & Training* – The management responsibility for the investment program is hereby delegated to the Chief Financial Officer, who shall establish written procedures for the operation of the investment program, consistent with this investment policy. Such procedures shall include explicit delegation of authority to persons responsible for investment transactions. The primary individual who shall be involved in investment activities will be the Chief Financial Officer. The Chief Financial Officer, Assistant to the Town Manager, and Accounting Manager are hereby designated as "Investment Officers" pursuant to the Public Funds Investment Act Section 2256.005 (f). Authority granted to a person to invest the funds on behalf of the Town shall remain in effect until rescinded by the Town or until the person resigns from or is terminated by the Town. The Chief Financial Officer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officers.

The Town shall provide periodic training in investments for the investment personnel through courses and seminars offered by professional organizations and associations in order to insure the quality and capability of the City's investment personnel. Such training shall be a minimum of ten hours within 12 months after taking office or assuming duties and thereafter no less than once in a two year period that begins on the first day of the Town's fiscal year and consists of two consecutive fiscal years after that date and receive not less than eight hours of instruction relating to investment responsibilities from an independent source and approved by the Town Investment Committee. Training must include education in investment controls, security risks, market risks, diversification of investment portfolio, and compliance with the Public Funds Investment. For purposes of this policy, an "independent source" from which investment training shall be obtained shall include a professional organization, an institute of higher learning or any other sponsor other than a business organization with whom the Town may engage in an investment transaction. Thus, these independent sources will be training sessions sponsored, accredited or endorsed by the Government Treasurers Organization of Texas (GTOT), Center for Public Management at the University of North Texas (UNT), Government Finance Officers Association of Texas (GFOAT), Texas Municipal League (TML), North Central Texas Council of Governments (NCTCOG), Association of Public Treasures United

States & Canada (APT US & C), and Government Finance Officers Association (GFOA).

No person may engage in investment transactions except as provided under the terms of this Policy. The Town Manager shall require an annual compliance review by an external auditor that will consist of an audit of management controls on investments, adherence to the Town's Investment Policy and a review of the quarterly investment reports. The reviews will provide internal control by assuring compliance with policies and procedures. The Town Manager, Chief Financial Officer, Assistant to the Town Manager, Accounting Manager and Town Council and other Finance Department employees shall be personally indemnified in the event of investment loss provided the Investment Policy has been followed.

B. *Conflicts of Interest* – All participants in the investment process shall seek to act responsibly as custodians of public assets. Officers and employees 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 their ability to make impartial investment decisions.

C. *Disclosure* – Anyone involved in investing Town funds shall file with the Investment Committee a statement disclosing any personal business relationship with a business organization offering to engage in investment transactions with the Town or is related within the second degree by affinity or consanguinity as determined under the Texas Government Code Chapter 573, to an individual seeking to transact investment business with the Town. A disclosure statement must also be filled with the Texas Ethics Commission and the Town Council. An Investment Officer or other employee has a personal relationship with a business organization if any one of the following three conditions are met:

1. The Investment Officer or employee owns 10% or more of the voting stock or shares of the business organization or owns $5,000 or more of the fair market value of the business organization.

2. Funds received by the Investment Officer or employee from the business organization exceed 10% of the investment officers gross income for the prior year.

3. The Investment Officer or employee has acquired from the business organization during the prior year investments with a book value of $2,500 or more for their personal account.

D. *Prudence* – The standard of prudence to be used by the investment officials shall be the "Prudent Person Rule", as set forth in Texas Government Code Section 2256.006, and will be applied in the context of managing an overall portfolio: "Investments shall be made with judgment and care under prevailing circumstances, that a person of prudence, discretion and intelligence would exercise in the management of the person's own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived."

Investment officials acting in accordance with the Investment Policy and exercising due diligence shall be relieved of personal responsibilities for an individual security's credit risk or market price change, provided deviations from expectations are reported in a timely manner and appropriate action is taken to control adverse developments. In determining whether an investment official has exercised prudence with respect to an investment decision, the determination shall be made taking into consideration the investment of all funds over which the official had responsibility rather than consideration as to the prudence of a single investment and whether the investment decision was consistent with the Town's Investment Policy.

E. *Reporting*

Quarterly – Not less than quarterly, the Chief Financial Officer shall submit to the Town Manager, Mayor and Town Council a written report of the Town's investment transactions within ninety (90) days of the preceding reporting period. The report shall: 1) describe in detail the investment position of the Town as of the end of the reporting period, 2) be prepared jointly by all Investment Officers, 3) be signed by each Investment Officer, 4) contain a summary statement, prepared in compliance with generally accepted accounting principles, of each pooled fund group including a) beginning market value for the reporting period; b) additions and changes to the market value during the period; c) ending market value for the period; d) fully accrued interest for the reporting period, 5) state the book value and market value of each separately invested asset at the beginning and end of the reporting period by type of asset and fund type invested, 6) state the maturity date of each separately invested asset that has a maturity date, 7) state the account or fund or pooled fund group for which each individual investment was acquired, and 8) state the compliance of the investment portfolio as it relates to the investment strategy expressed in the Investment Policy and with relevant provisions of the Texas Government Code Chapter 2256.

Annually – The Town Council shall review and approve the Investment Policy and investment strategy at least annually and be documented by rule, order, ordinance or resolution which shall include any changes made.

Compliance Audit – The Town's external independent auditor will conduct an annual review of the quarterly reports in conjunction with the annual financial audit. The results of the audit will be reported to the Town Council. The audit will also review compliance with management controls on investments and adherence to this Policy.

F. The guidelines of retaining records for seven years as recommended in the *Texas State Library Municipal Records Manual* should be followed. The Accounting Manager shall oversee the filing and/or storing of investment records.

G. Market prices for all public fund investments will be obtained and monitored through the use of an on-line data service such as Bloomberg, Interactive Data Inc. or a similar qualified successor agency. If the price of a particular security is not available from any of these sources, the price may be estimated by analyzing similar securities' market prices.

VII. SUITABLE AND AUTHORIZED INVESTMENT SECURITIES

A. *Active Portfolio Management* – The Town intends to pursue an active versus a passive investment management philosophy. That is, securities may be sold before they mature if market conditions present an opportunity for the Town to benefit from the trade. (Refer to Section VIII of this Policy.) In addition, the Investment Officers may at times restrict or prohibit the purchase of specific types of investments or issuers due to current market conditions.

The Town shall take all prudent measures consistent with this Investment Policy to liquidate an investment that no longer meets the required minimum rating standards, as per the Texas Government Code Section 2256.021. However, if it is determined by the Investment Committee that the Town would benefit from holding the securities to maturity to recapture its initial investment then the Investment Officers may act accordingly. The Town is not required to liquidate investments that were authorized investments at the time of purchase. (Texas Government Code Section 2256.017)

B. *Authorized Investments* – Town funds governed by this Policy may be invested in the instruments described below, all of which are authorized by the Public Funds Investment Act.

1. Obligations, including letters of credit, of the United States or its agencies and instrumentalities with stated maturities not to exceed five (5) years.

2. Direct obligations of this state or its agencies and instrumentalities with maturities not to exceed two (2) years.

3. Collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States, with maturities not to exceed two (2) years.

4. Other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, this state or the United States or their respective agencies and instrumentalities, including obligations that are fully guaranteed or insured by the Federal Deposit Insurance Corporation or by the explicit full faith and credit of the United States with maturities not to exceed two (2) years.

5. A certificate of deposit or share certificate is an authorized investment if the certificate is issued by a depository institution that has its main office or a branch office in this state and is:

    - Guaranteed or insured by the Federal Deposit Insurance Corporation or its successor or the National Credit Union Share Insurance Fund or its successor;

    - Secured by obligations that are described by Section 2256.009(a), including mortgage backed securities directly issued by a federal agency or instrumentality that have a market value of not less than the principal amount of the certificates, but excluding those mortgage backed securities of the nature described by Section 2256.009(b); or

    - Secured in any other manner and amount provided by law for deposits of the investing entity.

In addition to the Town's authority to invest funds in certificates of deposit and share certificates as stated above, an investment in certificates of deposit made in accordance with the following conditions is an authorized investment under Texas Government Code Section 2256.010 (b):

- The funds are invested by an investing entity through:
  - A broker that has its main office or a branch office in this state and is selected from a list adopted by the investing entity as required by Section 2256.025; or
  - A depository institution that has its main office or a branch office in this state and that is selected by the investing entity;

- The broker or the depository institution selected by the investing entity under Subdivision (1) arranges for the deposit of the funds in certificates of deposit in one or more federally insured depository institutions, wherever located, for the account of the investing entity;

- The full amount of the principal and accrued interest of each of the certificates of deposit is insured by the United States or an instrumentality of the United States; and

- The investing entity appoints the depository institution selected by the investing entity under Subdivision (1), an entity described by Section 2257.041(d), or a clearing broker-dealer registered with the Securities and Exchange Commission and operating pursuant to Securities and Exchange Commission Rule 15c3-3 (17 C.F.R. Section 240.15c3-3) as custodian for the investing entity with respect to the certificates of deposit issued for the account of the investing entity.

6. Investment Pools which invest in instruments and follow practices allowed by current law. A thorough investigation of the pool is required prior to investing, and on a continual basis. The Town Council must approve a formal agreement to participate (by Resolution) in each pool providing services to the Town. The pool must be continuously rated no lower than AAA or AAA-m or at an equivalent rating by at least one nationally recognized rating service.

   A public funds investment pool created to function as a money market mutual fund must mark its portfolio to market daily and, to the extent reasonably possible, stabilize at a $1 net asset value. Also, it must maintain a maximum average dollar-weighted maturity that does not exceed 90 days. Any investment pool that does not meet the requirements of one that is created to function as a money market mutual fund, must maintain a maximum average dollar-weighted maturity that does not exceed 365 days (or 366 days in the case of a leap year) and must provide a fixed interest rate and fixed maturity term for each pool position. The pool can only use money market mutual funds whose authorized investments are consistent with their own investment policy and authorized investments.

- To be eligible to receive funds from and invest funds for the Town, an investment pool must furnish to the investment officer or other authorized representative of the Town an offering circular or other similar disclosure instrument that contains, at a minimum, the following information:
  - 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; and
  - The performance history of the pool, including yield, average dollar-weighted maturities, and expense ratios.

- To maintain eligibility to receive funds from and invest funds for the Town, an investment pool must furnish to the investment officer or other authorized representative of the Town:
  - Investment transaction confirmations; and
  - A monthly report that contains, at a minimum, the following information:
    - The types and percentage breakdown of securities in which the pool is invested;

- The current average dollar-weighted maturity, based on the stated maturity date, of the pool;
- The current percentage of the pool's portfolio in investments that have stated maturities of more than one year;
- The book value versus the market value of the pool's portfolio, using amortized cost valuation;
- The size of the pool;
- The number of participants in the pool;
- The custodian bank that is safekeeping the assets of the pool;
- A listing of daily transaction activity of the entity participating in the pool;
- The yield and expense ratio of the pool, including a statement regarding how yield is calculated;
- The portfolio managers of the pool; and
- Any changes or addenda to the offering circular.

- The Town by contract may delegate to an investment pool the authority to hold legal title as custodian of investments purchased with its local funds.

- In this section, "yield" shall be calculated in accordance with regulations governing the registration of open-end management investment companies under the Investment Company Act of 1940, as promulgated from time to time by the federal Securities and Exchange Commission.

- If the ratio of the market value of the portfolio divided by the book value of the portfolio is less than 0.995 or greater than 1.005, portfolio holdings shall be sold as necessary to maintain the ratio between 0.995 and 1.005. In addition to the requirements of its investment policy and any other forms of reporting, a public funds investment pool created to function as a money market mutual fund shall report yield to its investors in accordance with regulations of the federal Securities and Exchange Commission applicable to reporting by money market funds.

- To be eligible to receive funds from and invest funds on behalf of the Town under this chapter, a public funds investment pool must have an advisory board composed:
    - Equally of participants in the pool and other persons who do not have a business relationship with the pool and are qualified to advise the pool, for a public funds investment pool created under Chapter 791 and managed by a state agency; or
    - Of participants in the pool and other persons who do not have a business relationship with the pool and are qualified to advise the pool, for other investment pools.

- If an investment pool offers fee breakpoints based on fund balances invested, the investment pool in advertising investment rates must include either all levels of return based on the breakpoints provided or state the lowest possible level of return based on the smallest level of funds invested.

Additionally, the pool must provide an annual audited financial statement of the investment pool in which the Town has funds invested and if the pool operates a website it must provide all information required in the offering circular 2256.016(b), monthly newsletter 2256.016(c)(2), and standardized SEC 7 day net yield 2256.016(f) on their website.

7. A Securities and Exchange Commission (SEC) registered, no load money market mutual fund which has a dollar weighted average stated maturity of 90 days or less and whose investment objectives includes the maintenance of a stable net asset value of $1 for each share. Furthermore, it must be rated not less than AAA, or an equivalent rating by at least one nationally recognized rating service and the Town must be provided with a prospectus and other information required by the SEC Act of 1934 or the Investment Company Act of 1940. The Town may not invest an amount that exceeds 10 percent of the total assets of any one fund; invest in the aggregate more than 15 percent of its monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service; or invest any portion of bond proceeds, reserves and funds held for debt service. Investments will be made in a money market mutual fund only after a thorough investigation of the fund and approval by the investment Committee which shall, at least annually, review, revise and adopt the money market mutual fund(s).

8. Commercial paper is an authorized investment if; (1) has a stated maturity of 270 days or fewer from the date of its issuance; and (2) is rated not less than A-1 or P-1 or an equivalent rating by at least: (A) two nationally recognized credit rating agencies; or (B) one nationally recognized credit rating agency and is fully

secured by an irrevocable letter of credit issued by a bank organized and existing under the laws of the United States or any state.

9. A guaranteed investment contract is an authorized investment for bond proceeds if the guaranteed investment contract:
    - Has a defined termination date;
    - Is secured by obligations described by Section 2256.009(a)(1), excluding those obligations described by Section 2256.009(b), in an amount at least equal to the amount of bond proceeds invested under the contract; and
    - Is pledged to the entity and deposited with the entity or with a third party selected and approved by the entity.

    Bond proceeds, other than bond proceeds representing reserves and funds maintained for debt service purposes, may not be invested in a guaranteed investment contract with a term of longer than five years from the date of issuance of the bonds.

    To be eligible as an authorized investment:
    - The governing body of the Town must specifically authorize guaranteed investment contracts as an eligible investment in the order, ordinance, or resolution authorizing the issuance of bonds;
    - The Town must receive bids from at least three separate providers with no material financial interest in the bonds from which proceeds were received;
    - The Town must purchase the highest yielding guaranteed investment contract for which a qualifying bid is received;
    - The price of the guaranteed investment contract must take into account the reasonably expected drawdown schedule for the bond proceeds to be invested; and
    - The provider must certify the administrative costs reasonably expected to be paid to third parties in connection with the guaranteed investment contract.

C. *Prohibited Investments* – The Town's authorized investment options are more restrictive than those allowed by State law. Not all investments authorized by State law are authorized by this Policy. Furthermore, this Policy specifically prohibits investment in the securities listed below:

1. Obligations, whose payments represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pays no principal;

2. Obligations whose payments represents the principal stream of cash flow from the underlying mortgage-backed security collateral and bears no interest;

3. Collateralized mortgage obligations that have a stated final maturity date of greater than 10 years;

4. Collateralized mortgage obligations the interest rate of which is determined by an index that adjusts opposite to the changes in a market index;

5. Bonds issued, assumed, or guaranteed by the State of Israel;

6. A fully collateralized repurchase agreement;

7. A securities lending program; and,

8. A bankers' acceptance.

Any other restricted instruments or limitations that involve outright speculation. The practice of "leveraging" whereby funds are borrowed for the sole purpose of investing shall not be practiced.

The Town is not required to liquidate investments that were authorized at the time of purchase. The Town will take prudent measures to liquidate any investment that loses its required rating.

D. *Diversification* – It is the policy of the Town to diversify its investment portfolios. The diversification will protect interest income from the volatility of interest rates and the avoidance of undue concentration of assets in a specific maturity sector; therefore, portfolio maturities shall be staggered. In establishing specific diversification strategies, the following general policies and constraints shall apply:

1. Risk of market price volatility shall be controlled by avoiding over-concentration of assets in specific maturity sector, limitation of average and final maturity and avoidance of over-concentration of specific instruments. All long-term maturities will be intended to cover long-term liabilities. Although there is no maximum defined portfolio liquidity position, it is the intent of this Policy to seek out higher yielding alternative investments in accordance with the prioritized objectives of preservation and safety of principal, meeting liquidity needs and yield enhancement as stated throughout the Public Funds Investment Act. To the extent possible, the Town will attempt to match its anticipated cash flow requirements with maturing investments.

2. The Investment Committee shall establish strategies and guidelines for the percentage of the total portfolio that may be invested in U.S. Treasury Securities, federal agencies/instrumentalities, and insured/collateralized certificates of deposit and other securities or obligations. The Investment Committee shall conduct a quarterly review of these guidelines, and shall evaluate the probability of market and default risk in various investment sectors as part of its considerations.

3. With the exception of U.S. Treasury securities and authorized pools, no more than 50% of the total investment portfolio will be invested in a single security type. (Such as FNMA, FHLB, FHLMC, CD's at one institution, etc.)

4. Risk of liquidity due to cash flow complications shall be controlled by maintaining minimum bank, investment pool, and money market mutual fund balances.

5. Purchases of securities with stated maturities greater than the maximum authorized under Section VIIB require prior Town Council approval.

VIII. SALE OF SECURITIES

The Town's policy is to hold all securities to maturity. However, securities may be sold to minimize the potential loss of principal on a security whose credit quality has declined, to swap into another security which would improve the quality, yield or target duration of the portfolio or to meet unanticipated liquidity needs. A horizon analysis is required for each swap proving benefit to the Town before the trade decision is made, and will be held in the file for record keeping.

IX. COMPETITIVE BIDDING

It is the policy of the Town to require competitive bidding for all individual security purchases and sales, as well as for certificates of deposit. Exceptions include:

A. Transactions with money market mutual funds and local government investment pools which are deemed to be made at prevailing market rates.

B. Treasury and agency securities purchased as new issues through an approved broker/dealer, financial institution or investment advisor.

C. Automatic overnight "sweep" transactions with the Town's depository bank.

At least three bids or offers must be solicited for all other transactions involving individual securities. The Town's investment advisor is also required to solicit at least three bids or offers when transacting trades on the Town's behalf. In situations where the exact security is not offered by other broker/dealers, offers on the closest comparable investment may be used to establish a fair market price for the security. In the case of a certificate of deposit purchase, at least two other offers should be solicited to provide a comparison. When few, if any, banks wish to participate then staff may use another authorized investment of similar maturity for evaluation purposes. The quotes may be accepted orally, in writing, electronically, or any combination of these methods. The Investment Committee may approve exceptions on a case by case basis or on a general basis in the form of guidelines. These guidelines shall take into consideration the investment type, maturity date, amount and potential disruptiveness to the Town's investment strategy.

X. ARBITRAGE

The Tax Reform Act of 1986 provided limitations restricting the Town's investment of tax-exempt bond proceeds. Revised arbitrage rebate provisions require that the Town compute earnings on investment from each issue of bonds on an annual basis to determine if a rebate is required. To determine the Town's arbitrage position, the Town is required to perform specific calculations relative to the actual yield earned on the investment of the funds and the yield that could have been earned if the funds had been invested at a rate equal to the yield on the bonds sold by the Town. The rebate provision states that periodically (not less than once every five years, and not later than sixty days after maturity of the bonds), the Town is required to pay the U.S. Treasury a rebate of excess earnings based on the Town's positive arbitrage position. The Tax Reform restrictions require precision in the monitoring and recording facets of investments as a whole, and particularly as they relate to yields and computations so as to insure compliance. Failure to comply may dictate that the bonds become taxable, retroactively from the date of issuance.

The Town's investment position, relative to the revised arbitrage restrictions, is the continued pursuit of maximizing yield on applicable investments while ensuring the safety of capital and liquidity. It is fiscally prudent to continue the maximization of yield and rebate excess earnings, if necessary.

XI. SELECTION OF BANKS, BROKER/DEALERS AND INVESTMENT ADVISORS

A. *Depository* – Town Council shall "select and designate one or more banking institutions as the depository for the monies and funds of the Town" in accordance with the requirement of Texas Local Government Code Chapter 105. The centralization of depository services is designed to maximize investment capabilities while minimizing service costs as well as staff time spent on activities such as reconciliation. At least every five years a depository shall be selected through the Town's banking services procurement process, which shall include a formal request for proposal (RFP). The selection of a depository will be determined by a competitive process and evaluated on the following criteria:

1. Qualified as a depository for public funds in accordance with state and local laws.

2. Provided requested information or financial statements for the periods specified.

3. Complied with all requirements in the banking RFP.

4. Completed responses to all required items on the proposal form.

5. Offered lowest net banking service cost, consistent with the ability to provide an appropriate level of service.

6. Met credit worthiness and financial standards.

B. *Investment Broker/Dealers* – If the Town has not retained an investment advisor, then the Investment Committee shall be responsible for adopting the list of qualified brokers/dealers and financial institutions authorized to engage in investment transactions with the Town. Authorized firms may include primary dealers or regional broker/dealers that qualify under SEC Rule 15C3-1 (uniform net capital rule) and qualified depositories as established by the Texas Local Government Code

Chapter 105. The Investment Committee shall base its evaluation of security broker/dealers and financial institutions upon:

1. Financial condition, strength and capability to fulfill commitments.

2. Overall reputation with other broker/dealers or investors.

3. Regulatory status of the broker/dealer.

4. Background and expertise of the individual representatives.

5. Ability to provide additional advisory services.

The Investment Committee must annually review the list of qualified broker/dealers authorized to engage in investment transactions with the Town. Investment Officers, or their authorized representatives, shall not conduct business with any firm whom public entities have sustained realized losses in investments or whose name the Investment Committee has removed from an approved list.

C. *Investment Advisor* – The Town may retain the services of an investment advisor firm registered under the Investment Advisor Act of 1940 (15 U.S.C. Section 80b-1 et seq.) or with the State Securities Board to assist in the review of cash flow requirements, the formulation of investment strategies, and the execution of security purchases, sales and deliveries. The investment advisors shall adhere to the spirit, philosophy and specific term of the Investment Policy and shall invest within the same objectives. The Investment Committee shall establish criteria to evaluate Investment Advisors, including:

1. Adherence to the Town's policies and strategies.

2. Investment strategy recommendations within accepted risk constraints.

3. Responsiveness to the Town's request for services and information.

4. Understanding of the inherent fiduciary responsibility of investing public funds.

5. Similarity in philosophy and strategy with the Town's objectives.

The investment advisory contract with the Town may not be for a term longer than two years and its renewal or extension must be approved by the Town Council by ordinance or resolution as required by the Texas Government Code Section 2256.003(b).

D. *Compliance* – A qualified representative from any firm offering to engage in investment transactions with the Town is required to sign a written instrument upon receiving and reviewing a copy of the Town's Investment Policy. Investments shall only be made with those business organizations (including money market mutual funds and local government investment pools) which have provided the Town with this written instrument executed by a qualified representative of the firm, acknowledging that the business organization has:

1. Received and reviewed the Town's Investment Policy.

2. Implemented reasonable procedures and controls in an effort to preclude investment transactions conducted between the Town and the organization that are not authorized by the Town's Investment Policy, except to the extent that this authorization is dependent on an analysis of the makeup of the Town's entire portfolio or requires an interpretation of subjective investment standards.

3. If the Town has contracted with an investment advisor, the advisor shall be responsible for performing financial due diligence on the Town's behalf. On an annual basis, the advisor will provide the Town with a list of its authorized broker/dealers, as well as the required written instrument described above.

4. As part of the annual audit, the independent auditor must formally review internal controls, compliance with the Policy, and the quarterly investment reports prepared to comply with the Public Funds Investment Act, and report the results of that review to the Town Council as part of its regular audit report.

XII. COLLATERALIZATION, SAFEKEEPING AND CUSTODY

A. *Collateralization* – The Town requires that all uninsured collected balances plus accrued interest, if any, in depository accounts be secured in accordance with the requirements of state law. Financial institutions serving as Town depositories will be required to sign a depository agreement with the Town which details eligible collateral, collateralization ratios, standards for collateral custody and control, collateral valuation, rights of substitution and conditions for agreement termination.

The Town requires that all uninsured certificates of deposit plus accrued interest held with a depository be secured in accordance with the agreement s of state law. Financial institutions will be required to sign a written depository and security agreement which stipulates eligible collateral, collateralization ratios, standards for collateral custody and control, collateral valuation, rights of substitution and conditions for agreement termination.

Collateral will always be held by an independent third party with which the Town has a current custodial agreement and shall be reviewed at least monthly to ensure that the market value of the pledged securities is adequate. All deposits and investments of Town funds, other than direct security purchases, money market mutual funds and local government investment pools shall be secured by pledged collateral set at no less than 102 percent of the market value of the principal and accrued interest on the deposits or investments less an amount insured by FDIC. Eligible collateral to secure the Town's deposits include:

1. Direct obligations of the United States government.

2. Other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, the United States government.

3. Direct obligations of agencies or instrumentalities of the United States government, including letter of credit.

4. Cash

The Town will reject adjustable rate mortgages (ARMs), collateralized mortgage obligations (CMOs), step-ups, variable rate instruments (except U.S. Treasury inflation protected securities), or securities that are not found on common pricing systems.

Additional collateral may be pledged as required, released when it is not needed, and substituted, if necessary, with the written consent of the Chief Financial Officer or Accounting Manager. Any financial institution requesting substitution must contact the Chief Financial Officer for approval and settlement. The substituted security's value will be calculated and substitution approved if its value is equal to or greater than the required security level. The Chief Financial Officer or Accounting Manager must provide a written notification of the decision to the bank or the safekeeping agent holding the security prior to any security release. Substitution is allowable for all transactions, but should be limited, if possible, to maximize potential administrative problems and transfer expense.

B. *Safekeeping and Custody* – Safekeeping and custody of the Town's investment securities shall be in accordance with state law. All security transactions, except local government investment pool and money market mutual fund transactions shall be conducted on a delivery versus payment (DVP) basis. That is, funds shall not be released or paid until verification has been made that the collateral or security was received by the Trustee or custodian. Investment securities will be held by a third party custodian designated by the Town, and be required to issue safekeeping confirmation notices clearly detailing that the securities are owned by the Town.

Safekeeping and custody of collateral pledged to the Town shall be in accordance with state law. Collateral will be held by a third party custodian designated by the Town. The custodian is required to issue safekeeping confirmation notices clearly showing that the securities are pledged to the Town.

C. *Subject to Audit* – All collateral shall be subject to inspection and audit by the Chief Financial Officer, or designee, as well as the Town's independent auditors.

XIII. MANAGEMENT AND INTERNAL CONTROLS

The Chief Financial Officer, or designee, shall establish and maintain a system of internal controls to ensure that the assets are protected from loss, theft or misuse. The internal controls shall be designed to prevent losses of public funds arising from fraud, employee error, and misrepresentation by third parties, unanticipated changes in financial markets, or imprudent actions by employees or Investment Officers of the Town. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived and the valuation of costs and benefits requires estimates and judgments by management.

Accordingly, the investment officer shall establish a process for an annual independent review by an external auditor to assure compliance with policies and procedures. Internal controls and managerial emphasis deemed most important that shall be employed include the following:

Imperative Controls

- Custodian safekeeping confirmation notices records management
- Avoidance or bearer-form securities
- Documentation of investment bidding events
- Written confirmation of telephone transactions
- Reconcilements and comparisons of security confirmation notices with investment records
- Compliance with Investment Policy
- Verification of all interest income and security purchase and sell computations

Controls Where Practical

- Control of Collusion
- Separation of duties
- Separation of transaction authority between Accounting and record-keeping
- Clear delegation of authority
- Accurate and timely reports
- Validation of investment maturity decisions with supporting cash flow data
- Adequate training and development of Investment Officers and staff authorized to execute investment transactions
- Review of financial conditions of all brokers/dealers and depository institutions
- Access to information about market conditions, changes and trends that require adjustments to investment strategies.

XIV. INVESTMENT POLICY ADOPTION

The Investment Policy shall be formally reviewed periodically by the Investment Committee and revised and recommended for Town Council approval, when necessary. In addition, the Investment Policy must be reviewed not less than annually by the Town Council. This review will include adoption of a written resolution stating that the Town Council has reviewed the Investment Policy and investment strategies and include any changes made to the Investment Policy and/or strategies in accordance with the provisions of the Public Funds Investment Act of the Texas Government Code Chapter 2256.

XV. INVESTMENT FINANCIAL GLOSSARY

Accretion
An accounting method for realizing the additional income earned through the purchase of a discounted, or zero coupon security where the difference between the discounted purchase price and the par value is credited to an income account, gradually increasing the book value until it reaches par at maturity. *Also see Amortization.*

Accrued Interest
An accounting term used to describe coupon interest earned, *but not yet paid* to the

security holder. Typically, an accounting entry is created to reflect the payable amount.

Agency: A category of investments that includes that Government Sponsored Enterprises (GSEs) of Fannie Mae, Freddie Mac, the Federal Home Loan Bank (FHLB) and the Federal Farm Credit Bank (FFCB). Federal agencies are generally considered to be *government securities* and all carry the highest possible senior debt rating from both Moody's and S&P.

American Call
A type of call provision whereby the issuer of a security has the right to return to the investor par value plus accrued interest at any time after a specific date has passed; also known as a continuous call.

Amortization
An accounting method for gradually reducing net income when a security is purchased at a premium, or a price that exceeds par. *See Accretion.*

Arbitrage
The profiting from the difference in price when the same security, currency or commodity is traded on two or more markets.

Arbitrage Bonds
Bonds issued by a municipality in the tax exempt markets and reinvested in the taxable markets in order to gain interest rate advantage or the advantage earned by refunding higher-rate bonds in advance of their call date. The proceeds from the lower-rate refunding issue are invested in treasuries until the first call date of the higher-rate issue being refunded.

Ask or Asking Price
The price at which securities are offered by the broker/dealer; the price at which a governmental entity buys a security; also referred to as an "offer" or "offering price".

Asset Allocation
The way that investments are distributed and weighted among different types of investment vehicles. The objective of asset allocation is to diversify market and credit risk while obtaining the greatest possible return consistent with the investors risk tolerance.

Asset-Backed Security (ABS)
A broad term used to describe a security created by pooling certain loans together, whereby principal and interest payments made on the loans are used to pay the security holders. Some common examples of ABS pools are auto loans and credit card receivables.

Bankers' Acceptance (BA)
A draft, bill or exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill as well as the issuer. Primarily, this is used in international trade.

Basis Point
The unit of measurement for yield equal to 1/100th of 1 percent; e.g., 1/4 of 1 percent is equal to 25 basis points.

Bear Market
A prolonged period of falling security prices usually caused by declining economic conditions and/or rising interest rates. A bear market may describe stocks or bonds, but it's important to remember that when bond prices are falling, yields are rising. A person may be "bearish" when they think investment prices will fall in the future, or if they have a negative outlook for the economy in general.

Benchmark
The performance of a predetermined group of securities, individual security or index used to compare risk and performance to a managed portfolio. A good benchmark should be verifiable, easy to understand and appropriate to the portfolio to which it is being compared. Typical benchmarks used in the public sector include the three-month, six-month and one-year T-bill averages over a similar measurement timeframe.

Bermuda Call
A type of call provision whereby the issuer of a security has the right to return to the investor par value plus accrued interest only on interest payment dates.

Bid
A bid is the price a broker will show an investor when the investor wishes to sell a security. An offer is the price a broker will show an investor who seeks to buy a security (also called the ask price). An investor will always seek the highest bid price when selling a coupon security, but will accept the lowest discount rate on a discounted security when selling. When buying securities we often refer to obtaining three competitive bids, actually we are getting 'competitive offers'.

Bond
A very broad term used to describe a debt obligation. A bond may have a fixed or floating coupon rate; may be issued by the U.S. Treasury or an agency or a corporation; and may be callable or non-callable.

Book Entry
The name given to securities whose ownership resides, and transfer occurs on a computer system. For treasuries and agencies this system is maintained by the Federal Reserve. Years ago, securities were traded in physical form similar to currency.

Book Value
The value at which a security is carried on an inventory list or other financial records of an investor. Book value reflects the principal price at which the security was originally bought plus/minus net amortization/accretion to that point in time. The book value *may* differ significantly from the security's current market value creating an unrealized gain or loss.

Broker
A broker brings buyers and sellers together in return for a commission (fee). Unlike a Dealer, the broker typically does not own the securities. Often times, the two are combined as "broker-dealer" because most may act in both capacities.

"Bullet"
Slang term for a type of bond that repays the entire principal amount on the maturity date. Bullets are never callable.

Bull Market
A market condition in which prices are rising; a bull market may describe stocks or bonds, but it's important to remember that when bond prices are rising, yields are falling. A person may be "bullish" when they think investment prices will rise in the future, or may be "bullish" in general if they have a positive outlook for the future economy.

"Buy-and-Hold"
A common investment strategy for conservative investors with specific cash flow objectives or cyclical cash flow patterns, whereby securities are purchased with no intention to sell prior to maturity.

Call Feature
Part of the agreement a bond issuer makes with a buyer, is called the indenture, describing the schedule and price of redemption before maturity. A call is an embedded option in the security allowing the seller to call (buy) it back at specific times.

Call Price
The price at which a bond or preferred stock with a call provision or call feature can be redeemed (repurchased) by the issuer. SEE Redemption Price

Call Provision
A bond provision that allows the bond issuer to redeem the bond prior to the bonds maturity date. If the bond states that this provision can be exercised after a given number of years, or at a price greater than the par value, or the bond is not callable, the bond is said to have call protection.

Call Risk
A form of investment risk that exists when a bond may be redeemed prior to maturity, leaving the investor to reinvest the principal at a lower yield. This risk increases when interest rates are falling, and it becomes more attractive for the bond issuers to call bonds

with higher interest rates and issue new bonds with lower interest rates.

Callable Security
A bond containing an option that grants the issuer of the bond the right to redeem the security early and return the full principal amount to the investor along with all accrued interest. The issuer will only call the bond if rates fall, at which time new bonds can be issued at lower rates. An investor in a callable security earns a higher yield, but is subject to reinvestment risk.

Capital Gain
The profitable result of the sale of a security or asset, whereby the principal amount exceeds the book value of the security.

Capital Loss
The resulting loss when the principal amount on the sale of a security or asset is less than the book value of the security.

Cash Flow Analysis
An analysis of changes in revenue and expenditures that affect the cash balance.

Cash Settlement
Cash settlement occurs when a security is purchased and subsequently delivered on the same day.

Certificate of Deposit (CD)
A time deposit that pays interest periodically or at maturity, a time deposit with a specific maturity evidenced by a certificate. Large denominations CDs are typically negotiable. There is a penalty for early withdrawal of the CD (time deposit).

"CHEAP" (vs. Expensive)
Slang term for securities that are trading at yield spreads higher than would be considered normal relative to similar security types or their own trading history.

CMO or Collateralized Mortgage Obligation
A derivative mortgage-backed security bond created from a large pool of home mortgage loans. A single CMO is divided into a number of different classes or "tranches", each containing unique risk profiles and characteristics. Most CMOs are not considered appropriate for local governments and other conservative investors.

Collateral
Securities, evidences of deposit, or other property that a borrower pledges to secure repayment of a loan; also refers to securities pledged by a bank or trade counter-party to secure deposits.

Commercial Paper (CP)
Unsecured, short-term obligations with maturities ranging from 1 to 270 days issued by banks, corporations and other borrowers to investors with large temporary cash positions. This type of security is usually issued at a discount and carries a zero coupon. The accounting process is identical to a T-bill. Prime commercial paper carries a short-term rating of A1 P1 or equivalent.

Compound Interest
The method of computing interest on a principle sum where the interest rate is applied to the original principle and any accumulated interest.

Constant Dollar Fund or Pool
A type of money market fund or investment pool whose stated objective is to offer safety of principal and liquidity by maintaining a $1 dollar share value for all its participants, meaning that the dollar value of the original deposit is expected to be maintained through conservative management practices; also referred to as a "dollar in / dollar out" fund or pool.

Continuous Call
A type of call option on a security in which the issuer maintains the right to repurchase the bond from the investor, at any time after the initial call date has passed. Also known as an American option.

Coupon Rate
The fixed annual rate of interest that a bonds issuer promises to pay the bondholder on the bonds face value. A certificate attached to a

bond evidencing interest due on a payment date.

Credit Risk
The risk that the issuer of a bond will default on its obligation to pay principal and/or interest when due. Credit risk is a primary consideration when purchasing commercial paper, banker's acceptances and corporate obligations.

CUSIP Number
CUSIP is the acronym for **Committee on Uniform Securities Identification Procedures**, and represents the standard industry identification for individual securities. Each security is assigned a unique CUSIP number.

Dated Date
Date at which interest begins accruing on a newly issued security. The dated date can sometimes differ from the issue date potentially causing accrual discrepancies.

Dealer
A dealer (as opposed to a broker) acts as a principal, by buying and selling for his or her own account. A dealer maintains a portfolio of securities and can trade from that portfolio. Often times, a "broker" will also act in a dealer capacity when selling securities owned by his or her own firm.

Debenture
A general term used to describe a bond secured only by the general credit of the issuer.

Deflation
A rare economic condition characterized by a general decline in prices of goods and services (the reverse of inflation). In a deflationary environment, fixed income securities become very desirable, pushing bond prices up and yields downward. During periods of deflation, there is a disincentive to produce.

Delivery versus Payment (DVP)
DVP requires that the delivery of securities is made at the same time payment for those securities is received in account.

Depository Trust Company (DTC)
A firm through which members can use a computer to arrange for securities to be delivered to other members without physical delivery of the certificates. The DTC uses computerized debit and credit entries. The system mirrors the FedWire system and was designed to reduce its load. When settling an investment that is DTC eligible, the delivering dealer will request the DTC number of the safekeeping agent.

Depreciation
The decline in the value of an asset or investment.

Derivative Security
A financial instrument whose value is based on, and determined by, another security or benchmark. Examples include mortgage back securities as well as Treasury strips, callable securities and floaters.

"Disco"
Slang term for an agency discount note.

Discount
The difference between the cost or the original purchase price of a security offered below par, and its PAR or face value.

Discount on Securities
The difference between a security's par value and its price when trading less than par price (100).

Discount Rate
The interest rate member banks pay the Federal Reserve when the banks use securities as collateral. Banks usually set their loan rates one point above the discount rate.

Discount Security
An agency note with a zero coupon issued to maturity dates not to exceed 365 days. This is a very common security type purchased by conservative institutional investors, public fund investment pools and money market fund portfolios.

Discrete Call
A call structure in which the option can be exercised only on specific dates; usually each quarter.

Disinflation
The slowing down of price increases, i.e. a slowing in the rate of inflation. Prices are still rising; they are just rising at a slowing rate.

Diversification
Dividing investable funds among a variety of different security types offering independent returns, and maturing at different times throughout the year(s). Diversification spreads an investor's risk and smoothes earnings. A well-diversified portfolio should perform relatively well regardless of the direction interest rates move.

Don't Know ("DK")
A term used in the securities clearance process when a bank or safekeeping agent will not accept delivery on a trade because it does not recognize the security being delivered

Duration
A measure of the price volatility of a bond equal to the weighted-average term to maturity of the bond's cash flows. The greater the duration of a bond, the greater its price volatility. The duration of a portfolio is roughly equivalent to the average maturity of the portfolio, and will vary depending on the size of the cash flows. If there are no actual cash flows, as in the case of a portfolio consisting of zero coupon T-bills or discount notes, the duration will equal the average maturity. Duration will be increasingly less than average maturity as the weighted average coupon of a portfolio increases.

European Call
A call structure in which the option may be exercised only on a single predetermined date; also known as a "one-time call".

Equity
Another name for "stock".

Fair Market Value
The likely market price for a security transaction between a willing, unbiased and non-desperate seller and a willing, unbiased and non-desperate buyer.

Federal Deposit Insurance Corporation (FDIC)
The federal agency that insures bank deposits, currently up to $100,000 per deposit as identified by taxpayer identification code.

Federal Funds
Funds deposited by commercial banks at Federal Reserve Banks, including funds in excess of bank reserve requirements.

Federal National Mortgage Association (FNMA) - Fannie Mae
FNMA was created in 1938 during the Great Depression to provide a secondary market for mortgage loans by purchasing groups of loans from lenders and packaging them into pools of mortgage-backed securities that can then sold to investors. To facilitate this process, Fannie Mae also issues debt in maturity ranges from one-day to 30 years. The company's long-term senior debt rating is currently AAA. Although Fannie Mae had operated as a private company since 1968, it was placed under Federal government conservatorship in September 2008 as a result of a significant decline the underlying market value of the mortgage loans it held and guaranteed.

Fed or Federal Reserve Bank
The Central Bank of the U.S. responsible for supervising and regulating member banks, providing banking services, providing information and setting monetary policy through the FOMC. Alan Greenspan was Fed Chairman from 1987 to January 2006. Ben Bernanke is the current Fed Chairman.

Federal Farm Credit Bank (FFCB)
A common issuer of agency securities; FFCB is part of the Farm Credit System, a nationwide network of borrower-owned institutions that lend to agricultural and rural America. The System was created in 1916 and is the oldest Government-sponsored enterprise (GSE). Unlike commercial banks,

System banks do not take deposits. Instead, funds for loans are obtained through the issuance of FFCB securities. Common FFCB securities include discount notes, debentures, callables and step-ups.

Federal Funds Rate
The rate of interest at which banks with excess reserves charge banks lacking reserves for overnight loans to meet reserve requirements. This key overnight rate determines, in large part, the rate at which overnight repurchase agreements will trade. When the Federal Reserve "raises rates", the target fed funds rate is increased and other short-term security yields follow. Since pools and money market funds invest heavily in short-term securities, their rates often approximate the fed funds rate at any given point in time.

Federal Home Loan Bank (FHLB) – A common issuer of agency securities, the Federal Home Loan Banks provide a source of low-cost funding to U.S. banks for all types of lending. With their members, the FHLBank System represents the largest collective source of home mortgage in the United States. The banks do not provide loans directly to individuals, only to other banks. Common FHLB securities include discount notes, debentures, callables and step-ups.

Federal Housing Administration (FHA)
A Federally sponsored agency that insures lenders against loss on residential mortgages.

Federal Housing Finance Agency (FHFA)
An independent government regulatory agency created in 2008 to oversee Fannie Mae, Freddie Mac and the Federal Home Loan Bank system. It effectively replaced the Office of Federal Housing Enterprise Oversight (OFHEO) and the Federal Housing Finance Board. James Lockhart was the first director, having served as the director of OFHEO. Its regulatory powers include the ability to place GSEs into government receivership or conservatorship if necessary. The FHFA placed Fannie Mae and Freddie Mac into conservatorship in September 2008.

Final Maturity
The date on which a security is due and payable. The maturity date stated on the face of the security.

Financial Industry Regulatory Authority (FINRA)
FINRA was formed through the merger of the National Association of Securities Dealers, Inc. (NASD) and the regulatory arm of the New York Stock Exchange. FINRA is a self-regulatory organization that is responsible for training, testing, licensing and oversight of registered broker dealers; arbitration and mediation; as well as regulation of the major U.S. stock exchanges.

Fixed Income Market
The market defined by securities with set (fixed) coupon rates.

Federal Open Market Committee (FOMC)
A group of Federal Reserve Officials that meet eight times per year to set U.S. monetary policy (raise and lower interest rates). The Committee must balance its two primary and often conflicting objectives of achieving stable economic growth and keeping inflation at acceptable levels.

FOMC – See Federal Open Market Committee

"Flex Repo" or Flexible Repurchase Agreement
A type of repurchase agreement used primarily for investment of bond proceeds that has a maturity date corresponding with the last expected construction draw for the bond project. Flex repos pay a fixed rate of interest and allow for cash withdrawals at the buyer's discretion during the life of the agreement.

Floater
A security whose value or coupon is reset on a periodic basis and moves up or down depending on the movement of a specified index like LIBOR or the 91- day T-bill yield.

Freddie Mac - the Federal Home Loan Mortgage Corporation (FHLMC) commonly referred to as "Freddie Mac" was created in 1970 to assist its sister company Fannie Mae by purchasing mortgage loans in the secondary market, pooling them together, and selling them to investors in the form of a mortgage-backed security. By providing a secondary market for home loans, Freddie Mac increases the amount of money available for mortgage lending. Like Fannie Mae, Freddie Mac issues debt in maturity ranges from one-day to 30 years. Its long-term senior debt rating is also AAA, and in September 2008, it too was placed under Federal government conservatorship as a result of a significant decline the underlying market value of the mortgage loans it held and guaranteed.

GAAP
Acronym for Generally Accepted Accounting Principles.

GASB
Acronym for the Governmental Accounting Standards Board.

GINNIE MAE (GNMA) or the Government National Mortgage Association.
GNMA buys Veterans Administration, Farmers Home Administration and Federal Housing Administration Mortgages, then issues bonds that are secured by pools of the mortgages. An investor in this type of bond receives monthly payments of principal and interest that represent monthly mortgage payments by homeowners. GNMAs are guaranteed by the full faith and credit of the U.S. Government unlike other agency mortgage-backed securities.

Government Bonds
A security issued by the U.S. Government and backed by its full faith and credit.

Inflation
The effect of generally rising prices of goods and services. Rising inflation will decrease the value of fixed income securities and push yields higher. The Fed seeks to control inflation by raising interest rates to slow the economy. Some degree of inflation is good - the Fed is generally thought to target an acceptable core inflation rate of approximately 2%.

Inflationary Risk
A form of investment risk that measures the effect of inflation on an investment. IF the after-tax return on an investment is lower than the rate of inflation, the investor will have less purchasing power at the maturity of the investment.

Instrumentality
A federal agency whose obligations, while note direct obligations of the U.S. Government, are sponsored or guaranteed by the government and backed by the government.

Interest Rate
The fixed annual rate of interest that a bonds issuer promises to pay the bondholder on the bonds face value.

Interest Rate Risk
A form of investment risk whereby changes in the general level of interest rates adversely affect the value of a security portfolio. For example, bond prices are likely to decline when market interest rates increase.

Inverted Yield Curve
A market condition where the yields on long-term securities are lower than yields on short-term securities. For example, the five-year Treasury-note yield is trading below the six–month Treasury-bill yield. An inverted curve typically occurs when investors expect rates

Issue Date
The date from which the bond begins to accrue interest. Also known as effective date.

Ladder
A common investment strategy whereby securities are purchased to mature at regular intervals so that cash is always available to meet known obligations, or be reinvested back into the market at prevailing yields.

LIBOR
Acronym for the London Interbank Offered Rate. In England's Eurodollar market,

LIBOR is the interest rate banks charge each other on short-term money; roughly equivalent to the Fed Funds rate in the U.S. In the U.S. market, LIBOR serves as a frequently used floating rate index.

Liquid Asset
Assets that can be converted easily into cash, some examples are money market fund shares, treasury bills and bank deposits.

Liquidity
The characteristic of an asset that allows it to be converted easily and quickly into cash without a substantial loss of value. Investment pools and money market funds are considered to be "fully liquid" since they can always be converted to cash on demand. Typically, the shorter the maturity, the more liquid the asset. Treasuries are considered the most liquid of all securities due to a continuously traded and efficient market.

Liquidity Diversification
An act of investing in bonds, which have different maturities.

Liquidity Risk
A type of investment risk whereby an investment may not be able to be sold quickly at a fair market price when cash is needed. Long-term Treasury Bonds, for example, are publicly traded and have excellent liquidity. Limited partnerships, on the other hand, are often not publicly traded and typically have poor liquidity.

LGIP
Acronym for Local Government Investment Pool. Very similar to a money market fund. Professionally managed portfolio of short-term securities owned on a pro rata basis by its local government participants.

"Long Bond"
Slang term for the most current issue of the 30-year Treasury bond.

Margin
The amount of additional collateral above 100% pledged to an entity in order to accommodate changes in market prices. A deposit or repo collateralized at 102% has a two-percent margin.

Market Risk
Risk that the price of a security will decrease with an overall decline in the market. This risk cannot be diversified away, but can be minimized by purchasing securities with shorter maturity dates. A decline in the market value of a security may not be considered a problem if that security can be held to maturity.

Market Value
The current value of a security determined by multiplying par value by the current market price. The unrealized gain or loss on a security can be calculated by subtracting the book value from the market value.

Master Repurchase (Repo) Agreement
The standard written agreement covering a repurchase or reverse repurchase agreement that establishes each party's rights in the transaction. A master agreement will 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 Account
A savings account which normally earns interest at a higher interest rate than a regular savings account, but with a minimum required balance and other restrictions.

Money Market Mutual Funds (MMMF)
A specific type of mutual fund that invest solely in money market instruments (short-term debt instruments, such as treasury bills, commercial paper, banker's acceptances, repos and federal funds) as defined and registered with the SEC and regulated by the Investment Company Act of 1940 as 2a-7 funds. They strive to maintain a $1 net share value for participants. Three types of MMMFs are Treasury, Governmental and Prime. MMMFs are designed for safety and liquidity.

Mortgage-Backed Security
A security backed by pools of home loan mortgages. Investors in mortgage-backed certificates receive monthly payments derived from the income stream of interest and principal on the underlying mortgages in the pool. A standard mortgage-backed security is referred to as a "pass-through". When a number of pass-through securities are combined and subsequently divided into separate classes of new securities with unique investment characteristics, these are called "collateralized mortgage obligations" or CMOs.

Municipal Bonds
A bond or debt obligation issued by state or local governments to fund general municipal needs or special projects. SEE Revenue Bonds

Mutual Fund
The fund pools the resources of investors who buy shares and invests the proceeds in a portfolio of securities designed to achieve the fund's investment objective. All of the owners in the fund shares participate in the gains and losses of the fund. The value of the share is calculated off the market value of the portfolio. These products can only be sold by registered representatives. Mutual funds are also known as an open-end diversified management investment company. Long term investment funds that pool money and can invest in a variety of securities, including fixed-income securities and money market instruments. Mutual funds are designed for yield and involve more risk than money market mutual funds. Mutual funds are regulated by the Investment Company Act of 1940 and must abide by the following Securities and Exchange Commission (SEC) disclosure guidelines.

National Association of Securities Dealers (NASD) – See Financial Industry Regulatory Authority (FINRA)

Net Asset Value (NAV)
The value of a mutual fund share as determined at the close of each business day. The NAV is determined by summing the market value of all securities in the portfolio, deducting expenses and dividing this total by the number of shares outstanding.

Net Asset Value Funds
A mutual fund seeking to offer a higher yield than the constant dollar funds (money market funds). These funds purchase longer maturing securities, which translate into a higher market and volatility risk as well as longer WAM. These funds experience market fluctuation due to the risk of the longer securities and will subject the investor to a higher level of market price and volatility risk than a constant dollar fund.

Normal Yield Curve
A yield curve where short-term yields are lower than long-term yields. The slope of the curve rises gradually in the early years and becomes almost flat in the latter years. Generally reflects a market in expectation of higher rates. Also known as Positive Yield Curve

Obligation
Any real debt.

Offer Price
The price at which investor will buy a security. When seeking to purchase a security, an investor will ask the broker for an offer.

Off-the-Run Securities
Previously issued Treasury securities not generally used for benchmarking or pricing purposes. They tend to be somewhat less active and less liquid than the most recent issues, but may offer more attractive yields as a result.

On-the-Run Securities
The most recently issued Treasury security in each maturity range. Often used as benchmarks. A Treasury yield curve will generally include "on-the runs".

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 Federal Open Market Committee (FOMC) in order to influence the

volume of money and credit in the economy. Open market operations are the primary tool that the Fed uses to raise and lower interest rates.

Opportunity Cost
The maximum profit an alternative plan of action would provide.

Overnight Repo
A type of repurchase agreement that is negotiated or renegotiated (rolled over) each day at a new interest rate. This investment type is heavily used by pools and money market funds. The daily repo rate tracks very closely with the fed funds target rate. Banks and dealers use repurchase agreements as a primary source of cash to finance their inventory positions.

Par Value
For bonds, the par value is the face amount on which interest is calculated and equals the amount of principal due at maturity.

Pledge Assets
Bank-owned securities used as collateral for government deposits. Authorized collateral is defined by the Public Funds Collateral Act of Texas.

Premium
1) The difference between a security's price and par (face amount) if the security is selling above its par value. 2) An amount that must be paid above par in order to call or refund an issue. 3) The price paid for an option.

Prepayment
The risk that changes in interest rates will cause the anticipated maturity of a mortgaged backed security to be shortened. Homeowners prepay all or part of a mortgage when interest rates decline to refinance at lower costs causing money to be returned to the owner of the mortgaged backed security who must reinvest at a lower rate.

Price/Book Ratio
A financial ratio, which relates a company's stock (share price) to its total assets less any intangible assets (goodwill, patents) minus current and long-term liabilities.

Price/Earnings Ratio
A financial ratio, which is commonly referred to as the P/E ratio or multiple. This is the relationship of a company's stock price divided by earnings per share. It provides stock investors with an indication of how much is being paid (share price) for a company's earnings potential.

Primary Dealer
A group of government securities dealers who submit daily reports of market activity and inventory positions to the Federal Reserve Bank of New York and are subject to its formal oversight. Primary dealers are required to "make a market" in U.S. Government securities, participate in Treasury auctions, provide the Fed with market information and analysis, and work with the Fed to implement monetary policy. A current list is available at – http://www.newyorkfed.org/markets/pridealers_current.html

Prime Rate
Rate of interest at which a commercial bank offers to lend money to its most creditworthy customers.

Private Activity Bond
A taxable municipal bond.

Proceeds
Money received from the sale of a security or from the issuance of a security.

Producer Price Index (PPI)
A measure of wholesale prices.

Promissory Note
An unconditional signed promise in writing to pay a specified sum in demand at a fixed time. A promise to pay.

Prudent Person Rule
An investment safety standard used by most governmental investors. The Rule states that investments will be made under circumstances then prevailing which persons of discretion and intelligence will purchase not for speculation but for investment recognizing the probable return of principal as well as the return on that investment.

Put
An option that gives the buyer of a security the right to sell that security back to the issuer (or put holder) at a specified time at a specified price.

Quantitative Easing
A method of increasing the money supply through open market operations of the Fed. Money is essentially created when the Central Bank purchases securities and credits the accounts of the sellers. With interest rates near zero, this is an alternative used by the Fed to free up credit for the financial markets.

Rally
A sharp rise in the general price level of the market, or a particular market or security; a rally implies higher prices for securities, and thus lower yields on fixed income securities. Example: "Stocks *rallied* today on better than expected earnings reports." Or "bonds *rallied* today after the Fed unexpectedly cut the target fed funds rate."

Rate of Return
A standard performance measurement that considers the coupon interest a security or portfolio of securities receives, along with any realized gain or loss, along with any change in unrealized market gain or loss. Depending on market volatility, the rate of return could differ significantly from the average yield of a portfolio.

Realized Gain/Loss
The true gain (profit) or loss of principal resulting from a sale of a security based on the difference between the security's book value and its market value. See Unrealized Gain/Loss.

Regular or "Reg" Settlement
Regular or "Reg" settlement is when cash and securities are exchanged on the day after trade date for Treasuries, agencies and commercial paper. Also see *Cash Settlement*.

Reinvestment Risk
The risk that funds will have to be reinvested in a security with a lower interest rate if the original security is called away.

"Repo" or Repurchase Agreement
A type of agreement in which an investor exchanges cash for securities with a primary dealer or bank and earns a fixed rate of interest for a specified period. At the end of the period, securities are returned for principal along with accrued interest. Dealers and banks use repo proceeds to finance their inventory positions.

Reset Date
The date on which a floating security's coupon rate is reset based on an established index and schedule

Revenue Bonds
Securities issued by governmental entities and secured by the revenue stream from the project being built or supported such as water treatment facilities or sewage plants.

"Reverse Repo" or Reverse Repurchase Agreement
The opposite side of a repo transaction. In a "reverse", the investor accepts cash from the dealer in exchange for securities, agreeing to return the principal with interest in exchange for the security at a later date.

Risk
A measure of the probability of financial loss.

Safe Harbor
The shifting of financial assets to less volatile areas to reduce risk. Example: When the stock markets crashes, fearful investors sell stocks and invest sale proceeds in the "safe harbor" offered by the U.S. Treasury market. This action is also referred to as a "flight to quality".

Safekeeping Location
A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the banks vault for protection.

Securities and Exchange Commission (SEC)
A governmental organization established to regulate the U.S. financial markets.

Secondary Market
A market existing for the purchase and sale of securities that were originally sold to investors days or even years earlier.

Securities Industry and Financial Markets Association (SIFMA)
SIFMA is a security industry trade group that represents banks, securities dealers, asset management companies in the U.S. and around the world. It was created by the merger of the Bond Market Association (BMA) and the Securities Industry Association. Its stated mission is to promote effective and efficient regulation, facilitate more open, competitive, and efficient global capital markets, champion investor education, retirement preparedness, and savings, as well as ensure the public's trust in the securities industry and financial markets.

Self-Regulatory Organization (SRO)
A stock exchange, securities, or commodities organization that is registered with Securities and Exchange Commission and that is responsible for making sure that its members obey rules and regulations.

"**Selling Off**" (sometimes known as "trading off")
A condition in which stock or bond prices move gradually lower following a rally.

Settlement Date
The purchase (or sale) date of a security on which the money actually changes hand (see also Trade Date)

Short
The practice of selling a security without owning it, in anticipation of subsequently purchasing it back at a lower price and making a profit. Not permitted by governmental entities.

Simple Interest
The method of computing interest on a principle sum where the interest rate is applied only to the original principal amount.

Skip Day Settlement
Skip Day or "Skip" settlement is when cash and securities are exchanged *two days after* trade date for Treasuries, agencies and commercial paper.

Spread
The difference between the current bid price and the current ask price of a given security, or between yields on similar securities; the additional yield over and above yields on Treasury securities, expressed in basis points, that can be earned by investing in non-Treasury securities.

When buying an agency, the offer will typically be presented in term of "spread to the comparable Treasury issue". For example, a two-year agency bullet may be offered at "plus 25 to the Treasury". What this means is that if the two-year Treasury note were yielding 1.00%, the agency would be offered 25 basis points higher to yield 1.25%.

Step-Up
A type of agency callable bond with a coupon rate that climbs higher as the security moves toward its maturity date. This security type offers some protection against rapid increases in interest rates, but may be called away before the coupon has a chance to "step" higher.

Strip
A security in which all the interest coupons have been removed, leaving only the principal. The new "strip" is a deeply discounted security which pays no interest, but returns all principal at maturity. The process of creating a principal strip also creates a corresponding interest strip. Although any fixed rate bond can be stripped, a Treasury strip is most common.

Swap
Trading one security for another with the objective of increasing overall return while maintaining similar risk and maturity characteristics in the new security. A typical swap may involve the sale of Treasury securities, which become expensive as they

near maturity, and the purchase of higher yielding discount notes or commercial paper.

Temporary Liquidity Guaranty Program (TLGP)
This program allows banks and certain other financial institutions to issue senior unsecured debt that carries an FDIC guarantee. Participating companies pay the FDIC a fee in exchange for the insurance. The FDIC's guarantee is backed by the full faith and credit of the United States.

Term Asset-Backed Loan Facility (TALF)
The Term Asset-Backed Securities Loan Facility (TALF) was announced in November, 2008, but working through the complicated operational details delayed the program until March 2009. The objective of the $1 trillion dollar program (originally $200 billion) is to free up funds for additional auto, student and small-business loans. The TALF hopes to accomplish this by encouraging big investors ($10 million minimum) to buy up newly issued AAA-rated pools of auto, student and business loans. Buyers pledge those securities as collateral in exchange for low-cost government funded loans of up to three years. The Wall Street Journal reported that prior to the beginning of the credit crisis, about 40% of consumer lending had been generated through the securitization process. At its peak, Wall Street issued $1 trillion a year in securities backed by consumer credit loans and trillions more backed by mortgages. In the final three months of 2008, only $8 billion in consumer loan-backed securities were issued. The Fed hopes the TALF program will reignite the securitization process and by extension the consumer lending market.

Term Repurchase Agreement
A repurchase agreement that lasts a longer than normal period of time, i.e. more than overnight.

Trade Date
The date on which the agreement to buy or sell a security is made (see also Settlement Date).

Treasury Bill
A highly liquid, short-term, US Government debt security issued at a discount from par value auctioned weekly by the U.S. Treasury with maturities ranging 30 days to 12 months. A Treasury bill is generally considered to be a risk-free investment.

Treasury Bond
A marketable, long-term, fixed coupon U.S. Government debt security with a maturity of more than 10 years.

Treasury Note
A marketable, medium-term, US Government debt security issued with a fixed coupon with an original maturity of two to 10 years.

Troubled Asset Relief Program (TARP)
After considerable debate, during what many considered to be an extremely dire liquidity crisis in the global financial markets, the TARP program became law on October 3, 2008. The original plan was for the U.S. Treasury to purchase or insure up to $700 billion of illiquid or "troubled" assets from banks and other financial institutions that were difficult to price because the secondary market had frozen up. A large number of these illiquid assets were mortgage-backed securities created by pooling together residential mortgage loans. When home foreclosures began to rise rapidly in 2008, the value of the mortgage-backed securities containing the troubled loans plummeted. Because there were virtually no ready buyers, it was nearly impossible to establish a fair trading market. The TARP was originally intended to purchase these illiquid assets, but the reality was that financial institutions were not willing to sell securities at severely distressed prices. On October 14, 2008, Treasury Secretary Paulson announced that the Treasury would instead purchase senior preferred stock and warrants in the nine largest American banks as well as in smaller banking institutions with the first $250 billion. The theory was that this would bolster the bank's capital positions, thereby enabling them to expand their lending activities. In reality, much of the capital

injected into these banks was gobbled up by growing losses.

Trust Indenture
A trust deed between a borrower and trust holder on the terms of the trust.

Underwriter
The firm that agrees to buy an issue of securities on a given date and at a given price who will then usually resell them through a distribution network.

Unrealized Gain or Loss
The amount of profit (or loss) that would be reflected on the sale of a security if that security were sold. The unrealized gain or loss is calculated by taking the difference between book value and market value of the security at a given point in time.

Variable Rate CD
Short term CD with an interest rate that is reset at set intervals on an agreed upon index.

Volatility
Characteristic of a security, commodity, or market to rise or fall sharply in price within a short-term period.

Weighted Average Maturity (WAM)
This common term, usually expressed in number of days, represents a dollar-weighted average of the remaining term to maturity of all assets in a pool or securities portfolio. A longer WAM generally indicates higher market risk. An SEC-registered money market fund has a 90-day WAM limitation, while a constant dollar investment pool is limited to a 60-day WAM.

Window
A term for the electronic bulletin board on which U.S. agencies sell their issues. The Agencies open their window for the initial offering of a security.

Yield
The return, expressed as a percentage, that a security will earn as a result of both the coupon rate and any discount earned or premium paid. A yield will exceed the coupon if purchased at a discount (and vice-versa).

Yield Burning
An illegal activity whereby a security provider charges more than the fair market price for a security, lowering the yield, thereby diverting arbitrage away from the IRS.

Yield Curve
The Relationship between yields and maturity dates for a set of similar bonds, usually Treasuries, at a given point in time. A yield curve is a standard measure of risk and return, and answers the question "how much additional yield will I earn if I extend my maturity and assume additional market risk?"

Yield-to-Call (YTC)
The expected yield to maturity of a bond if it is called on the scheduled exercise date.

Yield-to-Maturity (YTM)
The expected rate of return of a bond if it is held to its maturity date; calculated by taking into account the current market price, stated redemption value, coupon payments and time to maturity and assuming all coupons are reinvested at the same rate; equivalent to the internal rate of return (IRR).

Zero Coupon Bond
A bond that does not make interest payments but instead is sold at a deep discount. On the maturity date of the bond, the full-face amount is due. The difference between the amount paid at purchase and the face amount at maturity represents the income earned by the investor. Common examples of zero coupon bonds include Treasury strips, Treasury bills and agency discount notes.