



Office of the State Comptroller

INVESTMENT GUIDELINES FOR PUBLIC AUTHORITIES

A. INTRODUCTION

In accordance with Article X, Section 5 of the Constitution, the Comptroller is issuing these Investment Guidelines for Public Authorities to assist them in:

- establishing a prudent set of basic procedures to meet the individual investment objectives of each authority;
- assuring that investment assets are adequately safeguarded and collateralized;
- establishing and maintaining a system of internal controls including adequate accounts and records which accurately reflect in reasonable detail, all investment transactions; and
- providing for accurate reporting and evaluation of investment results in conformance with generally accepted accounting principles (GAAP).

All public authorities subject to the provisions of Part 201 of Title 2 of the Official Compilation of Codes, Rules and Regulations of the State of New York are required to comply with these investment guidelines. These guidelines contain certain fundamental principles and standards for the administration of an investment program. An investment program involving public funds must include four basic ingredients - legality, safety, liquidity and reasonable return. Section 2925 of the Public Authorities Law also requires public authorities to develop investment guidelines that meet certain basic requirements.

Because of the vast differences in the size and operations of public authorities and in the scope of their investment portfolios, these guidelines are intended to represent only minimum standards and be sufficiently broad to apply in most investment situations. It is the responsibility of each authority to determine and evaluate its own risks in all its investment transactions with due regard to prudent business principles and practices. In the final analysis, the decision to invest and the responsibility for prudence rests with the public authority officials. While individual public authorities are authorized to establish different systems and procedures that meet their specific needs in administering their investment programs, it is expected that all public authorities will meet the minimum standards contained in these guidelines. Any departure from these guidelines must be formally approved in writing by the governing board.

Public authority investments must be made in accordance with legal requirements. In addition, investments must be adequately protected and should generally be fully collateralized. The financial resources of the authority should be properly managed to achieve investment income consistent with sound investment practice. The following sections contain the essential elements that are generally recognized and accepted for the effective management and control of investments.

B. INVESTMENT POLICY

Each authority should have a written investment policy approved by its governing board. Members of the board should take an active role in the formulation of the investment policy. The investment policy should be reviewed periodically (at least annually) and revised as necessary to reflect changes in available investment opportunities and market conditions or as a result of any recommendations from the periodic evaluation of the performance of the investment program or any audits of the investment program.

The board may wish to delegate the formulation of the investment policy to an investment committee. In addition to formulating the investment policy, functions to be performed by the investment committee should include, but not be limited to, evaluating the investment program by:



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- (a) monitoring the system of internal controls;
- (b) verifying relevant matters relating to the securities purchased or held as collateral semi-annually and on an unscheduled basis;
- (c) determining that the investment results are consistent with the board's objectives; and
- (d) reviewing any independent audits of the investment program.

Investment policies should include the following:

1. Investment Objectives and Types of Investment Authorized

The primary investment objective of public entities is to earn reasonable rates of return. The investment policy should contain a detailed list of the permitted investments which shall be consistent with the appropriate provisions of the law relating to the authority, provisions of applicable note and bond resolutions and special policy directives of the board.

2. Diversification of Investments

The investment policy should include standards for the diversification of investments, both with respect to type of investment and firms with which the authority transacts business. Diversification policies might also address maturities.

3. Delegation of Investment Management

All investment transactions should be reviewed and approved by those officials designated by the board. The investment policy should list persons who are authorized to make investment decisions and should limit the number of persons who may place orders.

In some cases the State laws governing the operations of an authority may designate an official outside of the authority, such as the Commissioner of Taxation and Finance, to be the fiscal agent for the authority and to invest authority moneys not required for immediate use. Such a delegation does not relieve the authority from the responsibility of overseeing the investment program, since ultimately the board is responsible for the management and safeguarding of all the authority assets entrusted in its care.

4. Internal Control and Procedures

The organizational structure of the authority should wherever practical, provide for the separation of the authorization and accounting functions and both of these activities should be maintained separately from the custodial function.

The investment policy should include provisions requiring the investment officer to develop a detailed operating procedures manual which shall include:

- (a) the establishment and maintenance of a system of internal controls;
- (b) methods for adding, changing or deleting information contained in the investment record, including a description of the documents to be created and verification tests to be conducted;
- (c) a data base or record incorporating descriptions and amounts of investments, transaction dates, interest rates,



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maturities, bond ratings, market prices and related information necessary to manage the portfolio; and
(d) requirements for periodic reporting and a satisfactory level of accountability.

5. Selection of Investment Firms

An approved list of firms should be established for each type of investment based on applicable law and upon the qualifications of investment bankers, brokers, agents, dealers and other investment advisors and agents which transact business with the authority. The selection criteria should cover such factors as quality, reliability, experience, capitalization and size that in the judgment of the board make a firm qualified to transact business with the authority. When investing in repurchase agreements, dollar limits should be set for each firm.

6. Investment Procedures and Contracts

The authority's investment guidelines shall include procedures for each investment or transaction. Such procedures should include provisions:

- (a) deemed necessary and sufficient to secure in a satisfactory manner the authority's financial interest in each investment;
- (b) covering the use, type and amount of collateral or insurance for each investment;
- (c) establishing a method of valuation of collateral, and procedures for monitoring the valuation of such collateral on a regular basis and obtaining additional collateral when necessary to adequately secure investments; and
- (d) for the monitoring, control, deposit, and retention of investments and collateral which shall include, in the case of a repurchase agreement, a requirement that the obligations purchased be physically delivered for retention to the authority or its agent (which shall not be an agent of the party with whom the authority enters into such repurchase agreement), unless such obligations are issued in book-entry form, in which case the authority shall take such other action as may be necessary to obtain title to or a perfected security interest in such obligations.

The investment guidelines should include a requirement that the authority enter into a written contract for each investment, the provisions of which cover the items set forth in sub-paragraphs (a) through (d) above. If the authority shall determine by resolution that a written contract is not practical or that there is not a regular business practice of written contracts with respect to a specific investment or transaction, the procedures prescribed for that type of investment should nonetheless adhere to sub-paragraphs (a) through (d) above.

7. Collateralization

The investment policies should include provisions and procedures to fully secure or collateralize the authority's financial interest in investments, provided that the policy may include a description of the circumstances under which the authority's financial interest in investments may be less than fully secured. The collateral for investments should be limited to "investment grade" obligations (those permissible for direct investments). The collateral should be segregated in the authority's name and should be in the custody of the authority or a third party custodian. The authority should not accept a pledge of a proportionate interest in a pool of collateral. For demand deposits, time deposits and certificates of deposit, collateralization is required for amounts over and above Federal Deposit Insurance Corporation coverage. The market value and the accrued interest of the collateral should equal the value of the investment and any accrued interest at all times. The recorded value of the collateral backing any investment should be compared with current market values (mark-to-market) at the time of initial investment, and thereafter at least



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monthly, to be certain that it continues to be at least equal to the value of the investment plus accrued interest. For certain short-term investments the market value should be monitored on a daily basis. The mark-to-market reviews should use "bid" price from one constant source. It may be desirable to require collateralization in excess of the market value at the time of purchase. There should be a written custodial agreement which, among other things, specifies the circumstances under which collateral may be substituted and provides that the custodian is holding the securities solely for the benefit of the authority and makes no claim thereto.

8. Performance Evaluation and Audit

The investment policy should provide for the systematic and periodic evaluation of investment program compliance. This function may be performed by the board itself or assigned to the investment committee or the internal or external auditors. Section 2925 (3f) of the Public Authorities Law requires each authority to have an annual independent audit of all investments.

9. Reporting

The investment policy should explicitly require periodic reporting on the investment program including:

(a) Internal Management Reporting

There should be periodic (at least quarterly) reporting to the board on the investment program operations. Such reporting provides an effective tool for evaluating investment program compliance. Section 2925 (5) of the Public Authorities Law requires each authority to have prepared and filed with the board quarterly reports or reports covering such other period as may be approved by the board. The report or reports, from a designated officer or employee must indicate any new investments, the inventory of existing investments and the selection of investment bankers, brokers, agents, dealers, or auditors.

(b) Financial Statements

The authority's annual financial statements, which are required to be prepared in conformance with generally accepted accounting principles for governments (GAAP), should contain all of the note disclosures on deposits with financial institutions and investments required by the Governmental Accounting Standards Board (GASB) Statement No. 3, "Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements", dated April 1986. Other GASB Standards affecting investment reporting are GAS 28 on securities lending transactions, and GAS 31 on certain investments and external investment pools. In addition, GASB has issued an implementation guide and a technical bulletin (TB 87-01) clarifying the application of Statement 3. An additional technical bulletin (TB 94-1) has been issued requiring certain disclosures for transactions involving derivatives. Public authorities should review these standards and apply them as appropriate.

(c) Reporting to Oversight Agencies

Section 2925 (6 and 7(a)) of the Public Authorities Law requires an annual investment report to be submitted to the Division of the Budget with copies to the Office of the State Comptroller, the Senate Finance Committee, and the Assembly Ways and Means Committee. Such report shall include:



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- (1) the investment guidelines required by Section 2925 (3) and any amendments to such guidelines since the last investment report;
- (2) an explanation of the investment guidelines and amendments;
- (3) the results of the annual independent audit;
- (4) the investment income record of the authority; and
- (5) a list of the total fees, commissions or other charges paid to each investment banker, broker, agent, dealer and advisor rendering investment associated services to the authority since the last investment report.

C. OPERATING PROCEDURES

Operating procedures for the administration of an investment program should include the following:

1. The investment selection process should utilize competitive quotations or negotiated prices, except in the purchase of government securities at their initial value.
2. Each disbursement of funds (and corresponding receipt and securities) or delivery of securities (and corresponding receipt of funds) should be based upon proper written authorization. If the authorization is initially given verbally, there should be written or telegraphic confirmation from the investment officer to the custodian.
3. Payment of funds should only be made upon delivery of securities. Written confirmation of delivery should be obtained from the custodian.
4. The process of initiating, reviewing and approving requests to buy and sell investments should be documented and retained for audit purpose. Dealer limits should be established and reviewed regularly.
5. Custodians must have prior authorization from the authority to deliver obligations and collateral. All transactions must be confirmed in writing to the authority. Delivery of obligations sold should only be made upon receipt of funds.
6. Custodial banks should be required to report whenever activity has occurred in the authority's custodial account.
7. There should be at least monthly verifications of both the principal amount and the market values of all investments and collateral. Appropriate listings should be obtained from the custodian and compared against the authority's records.
8. A record of investments shall be maintained by the investment officer. The records should identify the security, the fund for which held, the place where kept, date of disposition and amount realized and the market value and custodian of collateral.

D. PROCEDURES FOR REPURCHASE AGREEMENTS

Great care must be exercised for those public authorities that invest in repurchase agreements. Because repurchase



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agreements may expose investors to serious risks, the following procedures should be followed to reduce those risks:

1. Repurchase agreements should only be purchased from banks or trust companies authorized to do business in the State of New York or from broker dealers on the Federal Reserve Bank of New York's list of primary government securities dealers.
2. Repurchase agreements should be for short periods of time. Agreements which are "open" (continuing in nature) should not be made.
3. The authority should execute a master repurchase agreement with each broker dealer which outlines the basic rights of both buyer and seller including:
 - (a) The events of default which would permit the purchaser and/or seller to liquidate or purchase the underlying securities;
 - (b) The relationship between parties to the agreement, which should ordinarily be purchaser and seller;
 - (c) A requirement that there be a written contract with the custodial bank outlining the responsibilities of the bank and the parties of the agreement. Such an agreement must provide, among other things, that the custodial bank will not make payment for the securities until the bank actually receives them and that the custodial bank takes possession of the securities exclusively for the authority and that any claims of the custodial bank are subordinate to those of the authority;
 - (d) Procedures which ensure that the authority obtains a perfected security interest in the securities which are the subject of the agreement;
 - (e) The method of computing margin maintenance requirements and providing for timely correction of margin deficiencies or excesses. Specific guidelines regarding margin maintenance should be established, taking in consideration:
 - (1) the size and terms of the transaction;
 - (2) the type of underlying security;
 - (3) the maturity of the underlying security;
 - (4) the capitalization, financial status and type of purchaser and/or seller; and
 - (5) the method by which additional margin will be maintained; and
 - (f) Circumstances, if any, under which substitution of securities subject to the agreement shall be permitted.
4. The authority or its custodian must take possession of the securities being purchased by physical delivery or book entry. The custodian should not be the same party that is selling the securities to the authority.
5. A custodial bank should be a member of the Federal Reserve Bank or maintain accounts with member banks to accomplish book-entry transfer of securities to the credit of the authority. Transfer of securities, whether by book entry or physical delivery, should be confirmed in writing to the authority by the custodial bank.
6. The market value of the securities purchased under a repurchase transaction must be equal to or in excess of the purchase price. The securities must be monitored and additional securities required if market fluctuations cause the market value of the purchased securities to become less than the purchase price.



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E. INDEPENDENT AUDIT CONSIDERATIONS

Section 2925 (3f) of the Public Authorities Law requires each authority to have an annual independent audit of all investments. The annual investment audit:

- (1) shall determine whether: the authority complies with its own investment policies; investment assets are adequately safeguarded; adequate accounts and records are maintained which accurately reflect all transactions and report on the disposition of authority investment assets; and a system of adequate internal controls is maintained;
- (2) shall determine whether the authority complied with the applicable laws, regulations and State Comptroller's Investment Guidelines; and
- (3) should be designed to the extent practical to satisfy both the common interests of the authority and the public officials accountable to others.

A written audit report should be prepared presenting the results of the annual independent audit of all investments and should include:

- (1) a description of the scope and objectives of the audit;
- (2) a statement that the audit was made in accordance with generally accepted government auditing standards;
- (3) a description of any material weaknesses found in the internal controls;
- (4) a description of all non-compliance with the authority's own investment policies as well as applicable laws, regulations and the State Comptroller's Investment Guidelines;
- (5) a statement of positive assurance of compliance on the items tested and negative assurance on those items not tested; and
- (6) a statement on any other material deficiency or finding identified during the audit not covered in (5) above.

In accordance with Part 201 of Title 2 of the Official Compilation Codes, Rules and Regulations of the State of New York, the audit report shall be filed within 90 days after the close of the authority's fiscal year with the Coordinator of Public Authority Programs, Office of the State Comptroller, A.E. Smith Office Building, Albany, New York, 12236.

F. EFFECTIVE DATE

The Investment Guidelines for Public Authorities are effective immediately and supersede the Short-Term Investment Guidelines for Public Authorities issued by the Office of the State Comptroller in March 1983.