

TOWN OF EAST GREENWICH
INVESTMENT POLICY

APPROVED SEPTEMBER 2008

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I. INVESTMENT RESPONSIBILITIES

A. Legal Requirements

1. Investment Authority

a) State Law

The Town of East Greenwich is a chartered municipality under P.L. 1973, ch. 157. As a result, the Town has full powers of self-government, including the power to invest Town funds.

b) Town Law

The authority to invest and deposit Town funds resides in the office of the Treasurer (Charter 4211).

2. Investment Policy

a) State Law

State law does not currently require the adoption of a formal investment policy. State law permits investments in a financial institution whose principal office is located in this state or which has a deposit taking facility within this state. Investments are also permitted in any mutual, money market fund comprised of government-backed instruments or repurchase agreements, provided that the ownership of shares is limited to the State or its instrumentalities (R.I.G.L. 35-10-11).

b) Town Law

The policies and procedures set forth in this document correspond to the state requirements and are considered essential to sound fiscal management.

3. Arbitrage

The Tax Reform Act of 1986 provides limitations on the Town's yield from investing tax-exempt General Obligation bond proceeds. These arbitrage rebate provisions require that the Town compute earnings on investments from each issue of bonds on an annual basis to determine if a rebate is required. To determine the Town's arbitrage position, the Finance Director will contract with the town's fiscal advisors to calculate the actual yield earned on the investment of the funds and compare it to the yield that would 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 provisions state that

periodically (not less than once every five years, and not later than sixty days after maturing of the bonds), the Town is required to pay the U.S. Treasury a rebate of any excess earnings. These restrictions require extreme precision in monitoring and record keeping, particularly in computing yields to ensure compliance. Failure to comply can result in the bonds becoming taxable, retroactive to the date of issuance.

The Town's investment position relative to the arbitrage restrictions is to continue pursuing the maximum yield on applicable investments while ensuring the safety of capital and liquidity. To continue maximization of yield and rebate excess earnings, if any, is a fiscally sound position.

II. INVESTMENT OBJECTIVES

A. Safety of Capital

Considering the portfolio as a whole, the foremost objective of the Town of East Greenwich is to ensure the safety of principal. Specific policies that ensure the safety of principal are presented in section III.A. "Safety of Principal."

B. Maintenance of Adequate Liquidity

The Town's investment portfolio must be structured in a manner that will provide the liquidity necessary to pay obligations as they become due. Specific policies that ensure maintenance of adequate liquidity are described in section III.B. "Adequate Liquidity."

C. Return on Investments

Consistent with State law, the Town shall seek to optimize return on investments within the constraints of safety and liquidity. Specific policies regarding investment rate of return are presented in section III.C. "Achieving Investment Return Objectives."

D. Prudence and Ethical Standards

The standard of prudence used by the Town of East Greenwich shall be the "prudent person" and shall be applied in the context of managing an overall portfolio. The prudent person rule is restated below:

In acquiring, investing, reinvesting, exchanging, retaining, selling and managing property for any trust heretofore or hereafter created, the Town of East Greenwich will exercise the judgment and care under the circumstances then prevailing which persons of prudence, discretion and intelligence exercise in regard to the permanent disposition of their funds, considering the probable income as the probable safety of their capital.

Specific policies describing the Town's prudence and ethical standards are delineated in section III.D. "Ethical and Prudent Action."

III. INVESTMENT POLICIES

A. Safety of Principal

Ensuring safety of principal is accomplished by limiting two types of risk: (1) credit risk and (2) interest rate risk. Credit risk is the risk of loss associated with the failure of a security issuer or backer. Interest rate risk is the risk that the value of the portfolio will decline due to an increase in the general level of interest rates.

1. Reducing Credit Risk – Investments

a) Acceptable Investments

The Town's policy is to purchase only obligations of the United States government and its agencies, fully collateralized, direct repurchase agreements secured by obligations of the U.S. government and its agencies, and certificates of deposit in financial institutions meeting the Town's standards for credit worthiness.

The Town may purchase government and agency obligations through brokers, dealers or banks or via a money market fund dealing exclusively in Government and Agency obligations provided by an investment company meeting the criteria of R.I.G.L. 35-10-11. Repurchase agreements and certificates of deposit may be purchased from financial institutions, brokers or agents.

The Finance Director will diversify investments between financial institutions such that 50% of the Town's average monthly expenses will be invested in a second financial institution. This will ensure that access to adequate funds will be maintained in the event that delays occur in collateral redemption at one institution.

Commercial paper, instruments not specifically authorized by this document and mutual money market funds investing in more than Government and Agency obligations or repurchase agreements will not be purchased.

Items (5) through (14) below are considered instrumentalities of the U.S. government and are therefore considered as investment grade securities for public funds. Item (15) below is secured by the full faith and credit of the U.S. government. The Finance Director may at times prohibit purchase of specific issues due to prevailing market conditions. The following are considered acceptable investments:

(1) United States Treasury Bills

Short-term obligations of the U.S. government, issued and sold at a discount, with maturities of 13, 26 and 52 weeks.

(2) United States Treasury Notes and Bonds

Obligations of the U.S. government with a fixed coupon rate and original maturities of one year or more.

(3) Repurchase Agreements

Contractual agreements between the Town and brokerage firms, banks or government bond dealers. The repurchase agreement (repo) issuer receives cash and, in turn, provides securities as collateral for the cash. There exists a contractual agreement for the repo issuer to repurchase the securities at predetermined dates and prices. The right of substitution of collateral may be granted by the Finance Director.

(4) Money Market Mutual Funds

Funds offered by companies which meet the criteria of R.I.G.L. 35-10-11 and which invest **exclusively** in U.S. Government and Agency obligations and repurchase agreements.

(5) Federal Farm Credit Bank Debentures

Consolidated obligations for the Farm Credit Banks, issued on a discount basis, with maturities of one year or less.

(6) Federal Farm Credit Bank Debentures

Consolidated obligations of the Farm Credit Banks, issued with a fixed coupon rate, with maturities ranging from six months to twenty years.

(7) Federal Home Loan Bank Discount Notes

Consolidated obligations of the twelve district banks, issued on a discount basis, with maturities of one year or less.

(8) Federal Home Loan Bank Debentures

Consolidated obligations of the twelve district banks, issued with a fixed coupon rate, with maturities ranging from one to ten years.

(9) Federal National Mortgage Association Discount Notes

Obligations of the Association, issued on a discount basis, with maturities under one year.

(10) Federal National Mortgage Association Debentures

Obligations of the Association, issued with a fixed coupon rate, with various maturities.

(11) Federal Home Loan Mortgage Corporation

Obligations of the Corporation, issued on a discount basis, with maturities under one year.

(12) Federal Home Loan Mortgage Corporation Debentures

Obligations of the Corporation, issued with a fixed coupon rate, with various maturities.

(13) Federal National Mortgage Association Mortgage Backed Securities

Issues of the Association, representing undivided interests in conventional mortgages underwritten and previously purchased by the Association. The Association guarantees the timely payment of interest at the certificate rate and full return of principal. Original maturity payment dates are thirty years.

(14) Federal Home Loan Mortgage Corporation Participation Certificates

Issues of the Corporation, representing undivided interests in conventional mortgages underwritten and previously purchased by the Corporation. The Corporation guarantees the timely payment of interest at the certificate rate and full return of principal. Original maturity payment dates are thirty years.

(15) Governmental National Mortgage Association Pass-Through Securities

Issues of the wholly-owned governmental corporation within the Department of Housing and Urban Development. Principal and interest payments collected on mortgages in specified pools are passed through to holders of GNMA-

guaranteed certificates after deduction of servicing and guaranty fees. Original stated maturities are twelve to forty years.

b) Approved Brokers/Dealers/Financial Institutions

The Town's policy is to purchase securities only from those institutions included on the Town's approved list of brokers, dealers and financial institutions. To be included on the approved list, financial institutions, dealers and brokers must meet the standards set forth in section IV.C. "Selection Criteria for Financial Institutions, Brokers and Dealers." The Town shall limit trading to organizations that require a written agreement for their records of individuals authorized to transact business for the Town. The Town trading authorization will designate the Town Manager and Finance Director as authorized to invest for the Town. These same officials are authorized to sign all investment related agreements on behalf of the Town.

c) Safekeeping of Securities

(1) Safekeeping Agreement

The Town shall sign a master repurchase agreement with a bank or banks for the safekeeping of securities held as collateral to secure repurchase agreements.

(2) Verification of Security

Verification of collateral and insured investments will be part of the Town's annual independent audit.

d) Collateralization

The Town's policy is to require full collateralization of all Town investments and funds on deposit with a depository bank, other than investments in obligations of the U.S. government and its agencies or a money market fund that invests exclusively in Government and agency obligations. However, due to the check "float" or a minimum retention threshold for sweep accounts that may exceed the \$100,000 maximum for insurance coverage, a portion of the investments may be neither collateralized nor insured. The Finance Director will strive to keep this portion to a minimum.

(1) Allowable Collateral

Repurchase agreements. Collateral underlying repurchase agreements is limited to U.S. government and agency obligations.

(2) Collateral Levels

Collateral is valued at current market plus interest accrued through the date of valuation.

Repurchase agreement collateral must be maintained at the following minimum levels, with respect to repurchase agreement par value plus accrued interest:

1 year or less 102%

(3) Monitoring Collateral Adequacy

Repurchase agreements. The Town’s policy is to require bi-weekly monitoring of all collateral underlying repurchase agreements whose duration exceeds 30 days.

(4) Margin Calls

Repurchase agreements. If the value of the collateral underlying a repurchase agreement falls below the margin levels specified in III.A.1.(d)(2) above, the Finance Director will make a margin call unless the repurchase agreement is scheduled to mature within five business days or the amount is deemed to be inconsequential.

(5) Collateral Substitution

Collateralized investments occasionally require substitution of collateral. Any broker or financial institution requesting substitution must contact the Finance Director for approval and settlement. The substituted collateral’s value will be calculated and the substitution approved if its value is equal to or greater than the original’s.

e) Bid Monitoring

The Town’s policy is to document all bids offered on all types of securities. A minimum of three bids will be taken on all investments over one million dollars (\$1,000,000), except where the governmental instrument being purchased has its rate set at public auction.

f) Portfolio Diversification

To enhance the total yield and fulfill investment policy objectives, the investment management style will be directed towards an active rather than passive portfolio. Market risk shall be minimized by diversification of investment types.

The following maximum limits, by instrument, are established for the Town's total portfolio:

1.	Repurchase Agreements (collateralized)	100%
2.	Certificates of Deposit	90%
3.	U.S. Treasury Notes/Bonds/Bills	100%
4.	U.S. Agencies	60%
5.	Money market funds (invested exclusively in government and agency obligations)	70%

The Town's policy is to diversify its investment portfolio to minimize the risk inherent in over-concentration in a specific investment instrument or depository.

g) Master Repurchase Agreement

The Town's policy is to require each issuer of repurchase agreements to sign a Master Repurchase Agreement.

2. Limiting Interest Rate Risk

The longer the maturity of bonds, the greater their price volatility. Therefore, the Town's policy is to concentrate its investment portfolio in shorter-term securities to limit principal risk caused by changes in interest rates. The weighted average days to maturity for the Town's General and Sewer Funds invested must be less than 365 days.

B. Adequate Liquidity

The policies set forth in this section are intended to maintain the liquidity necessary to meet the Town's demands for cash.

1. Repurchase Agreement Maturities

Since no secondary market exists for repurchase agreements, the maximum maturity for repurchase agreements shall be 120 days.

2. Security Marketability

Only U.S. government and agency obligations with active secondary markets will be purchased. Marketability shall be determined by the Finance Director.

C. Achieving Investment Return Objectives

The policies set forth in this section will enable the Town to achieve the yield objectives established for the portfolio.

1. Active Portfolio Management

The Town's policy is to actively manage the investment portfolio to enhance overall interest income. Through active fund management,

rather than a “buy-and-hold” strategy, portfolio yield may be enhanced with minimal increase in risk. Active management will take place only if prudent within the context of the “Prudent Person Rule.” (See section II.D.)

2. Portfolio Maturing Management

When structuring the maturity composition of the portfolio, the Finance Director will follow the Town’s policy of evaluating current and expected interest rate yields. The longer the time remaining to maturity for a security, the greater the price fluctuation, given a change in interest rate levels.

3. Competitive Bidding

The Town’s policy is to require competitive bidding for all investment purchases in excess of \$1,000,000, except where the governmental instrument being purchased has its rate set at public auction. At least three bids must be obtained for these types of investments. All bids must be documented for auditing purchases. In the case of tie bids, the Finance Director will make the investment-award decision, giving preference to the institution holding the maturing investment (to avoid wire transfer charges).

D. Ethical and Prudent Action

1. Prudent Investment Management

The Town’s investment policy intends that the Finance Director perform his/her duties in accordance with the policies and procedures expressed in this document. In the absence of the Finance Director, the Town Manager is to effect investments in accordance with this document.

2. Standards of Ethics

The Finance Director and Town Manager, as custodians of the public trust, will adhere to the highest personal standards of ethical conduct. As investment officials they shall avoid any transaction that might impair public confidence in the Town’s ability to govern effectively. Town employees involved in the investment process shall refrain from personal business activity or investments that could impair their ability to make impartial investment decisions. Investment officials shall disclose to the Town Council any material interests in financial institutions that conduct business with the Town, and shall further disclose any material personal investment positions that could be related to the performance of the Town’s investment portfolio.

3. Training and Education

The Town's policy is to provide periodic training in investments for the Finance Director through courses and seminars offered by the Government Finance Officers Association and similar professional organizations.

E. Banking Services

The Town of East Greenwich will, through a request for proposal process as required by R.I.G.L. 45-55, designate one bank as its primary depository for financial services. This centralization of banking services is designed to maximize investment capabilities and minimize banking cost. The depository designation does not limit investment activity to the one designated financial institution, but provides that the major accounts will be maintained at that institution.

Considerations the Town of East Greenwich will use to consummate a banking services contract will include the following:

1. Full service capability, including zero balance accounts and sweep accounts;
2. Submission of financial statements;
3. Monthly statements of compensating balances;
4. Compliance with financial qualifications per section IV.C;
5. Statement of staff experience;
6. Statement on equal employment opportunity practices;
7. Demonstration of comparable processing volume.

Selection of the financial institution, by the Town Manager, shall be based upon the lowest, qualified evaluated bid.

No time length for Town banking service contracts is required by State law. The Town's contract shall not exceed four years with annual performance reviews a necessary proviso. Special banking needs may be contracted outside this policy if approved by the Finance Director and Town Manager. If a financial institution drops below the Town's standards of financial stability pursuant to section IV.C.1, the bank will be required to meet the requirements within six months or lose its banking services contract.

IV. INVESTMENT OPERATING PROCEDURES

A. Investment Program Development

1. Overview

The investments of the Town of East Greenwich are administered according to the investment policy which will be evaluated by the Town Manager and Finance Board annually.

2. Operations

The investment policy should contain the following:

- a. Summarize economic and market analyses;
- b. Forecast available cash for investment;
- c. Access compliance with insurance and collateralization requirements;
- d. Formulate strategies concerning:
 - i. asset mix;
 - ii. investment instruments;
 - iii. maturities;
 - iv. target yields;
- e. Report performance to the Town Council and Finance Board semi-annually.

B. Market and Economic Analysis

The Finance Director will be responsible for routinely performing market and economic analyses to support investment strategy and planning. These analyses will be performed using information obtained from investment advisors and brokers, as well as the original data. The objective of the market and economic analysis will be to forecast probable market conditions for the period for which investments are planned.

C. Selection Criteria for Financial Institutions, Brokers and Dealers

1. Selection Criteria for Banks and Credit Unions

a) Overview

A financial institution must meet the minimum criteria outlined below.

Bank rating criteria are calculated using publicly available financial information obtained from preliminary reports of condition and

reports on income from the Federal government. Factors evaluated will include capital adequacy, asset quality, earnings and liquidity.

b) Minimum Criteria for Selection

The Town Manager may approve a bank or credit union if all of the following criteria are met:

1. The financial institution must be insured by the FDIC or the NCUA.
2. Only financial institutions incorporated under the laws of the State of Rhode Island or of the United States shall be appointed as depositories of the Town funds.
3. A qualified depository must meet the financial criteria specified in R.I.G.L. 35-10. A qualified depository must also exceed the minimum primary capital adequacy guidelines for its size established by the Federal Reserve Bank by one full percent and have a non-performing asset-to-total-loans ratio of no greater than 5%. In addition, the Finance Director will periodically consult various bank rating agency reports to ensure that banks that are on the approved list have not been ranked in the ‘warning’ category. Should this event occur, the Finance Director will expeditiously transfer funds to another financial institution.
4. A financial institution found to be in violation of fair lending laws or the federal Community Reinvestment Act (CFA) will be removed from the list until the situation has been remedied. For a bank which is already on the list, the Finance Director, weighing early withdrawal penalty, will review investments for transfer to another institution as soon as practical.

2. Selection Criteria for Brokers/Dealers

The Finance Director shall maintain an approved list of securities brokers/dealers with whom the Town may conduct security transactions. Only those brokers/dealers on the approved list are entitled to submit quotations and transact business with the Town. Any broker/dealer failing to maintain the minimum criteria outlined below will be deleted from the approved list.

a) Approved Brokers/Dealers

Only approved brokers/dealers will be used for investment transactions. Brokers/dealers must be regulated by the Securities and Exchange Commission (SEC), and be members in good

standing of the National Association of Securities Dealers, Inc. (NASD). Commissions charged should conform to industry standards and not exceed \$500 annually.

b) Broker/Dealer – limited numbers

There are no limits on the number of dealers or brokers with whom the Town may do business.

c) Removal from Approved List

In, if the judgment of the Finance Director or Town Manager, a broker/dealer is considered to place the Town's investments at risk, removal from the approved list may be made immediately.

D. Instrument Selection

1. Liquidity Needs

Investments are usually selected according to anticipated cash needs. For example, investments made for the General Fund may be placed in securities with maturities prior to anticipated cash needs with the objective of taking advantage of yield curves and earning additional returns.

2. Portfolio Structure and Policy Guidelines

The Finance Director will consider the composition of the current portfolio and determine whether the securities being considered will maintain the portfolio within policy guidelines.

3. Current and Expected Yield Curve Analysis

The Finance Director will monitor current and expected yield curves. When interest rates are expected to decline, consideration will be given to extending maturing ranges within portfolio and policy constraints. When interest rates are expected to increase, consideration will be given to shortening maturing ranges.

4. Yield Spread Analysis

The Finance Director will monitor yield spreads between various government agency issues and U.S. notes and bonds.

V. PERFORMANCE EVALUATION AND REPORTING

Investment performance is continually monitored and evaluated by the Finance Director. The Finance Director will produce summary reports on a monthly basis for the Town Manager.

A. Monthly Performance Analysis

The following reports will be produced monthly for presentation to the Town Manager, Finance Board and Town Council:

1. Month-end Portfolio

The month-end portfolio will be displayed by type of investment within fund. The report will include market values and interest rate for each security. The report will be provided by the 20th of the month following the report month.

B. Changes to the Investment Policy

Although not currently required by state law to enact an investment policy, the Town Council has decided that prudent investment management requires explicit policies and procedures. After adoption of this policy document, the Town Council must approve any subsequent revisions.