WASHINGTON STATE ASSOCIATION OF COUNTY TREASURERS

INVESTMENT BEST PRACTICES

OUR MISSION

To provide a forum for all county treasurers to educate, advocate, mentor and support the creation of effective treasury management systems which honor the public trust.

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WSACT INVESTMENT BEST PRACTICES RECOMMENDATIONS

County Treasurers in Washington State have a fiduciary responsibility in managing the funds of the elected offices, departments, and districts where they serve. This includes the important work of ongoing management and monitoring of investment activities. In the following sections, we cover the key factors that should be at the forefront of all investing decisions, as recommended by the Washington State Association of County Treasurers (WSACT). We will briefly outline these factors to provide a better understanding of how to structure an investment strategy and develop a concise investment policy tailored to a county's investment needs.

1. Policies to Govern the County's Investing Practices

A prudent investment strategy should be anchored by a well-structured formal Investment Policy and supported by written procedures. Per RCW 36.48.070 all counties must formally adopt a comprehensive written investment policy. It is recommended that these policies are reviewed and updated annually or every four years at a minimum. The investment policy should be approved by the Washington Public Treasurers Association (WPTA) or other organizations recognized as a leader in investment policy (see page **5** for specific guidelines). Pooling counties should have a formal Pool Participant Resolution or Participation Agreement. The Agreement should be amended anytime material changes are made to investment methods or other activities, such as transaction or calculation parameters. Terms of the agreements are based on each county's needs.

2. Cash Flow Forecasting

All counties should develop reasonable expectations of timing and amounts of planned expenditures. Historical and known data should be used to measure activity of a cyclical nature, for both receipts and disbursements, considering one-time or anomalies in revenue and expenses. Forecasts should be updated regularly based on the county's needs. These forecasts should consider necessary reserve levels based on liquidity needs that account for expected inflows and outflows during a given period (for resources, see **Appendix A**).

3. Portfolio Diversification

Portfolio diversification is key to helping counties manage risk. Counties need to establish a risk profile which takes into consideration limitations established by state statute, investment objectives and constraints, risk tolerances, liquidity requirements, expertise available, and the current risk/reward characteristics of the market.

Interest rate risk is managed by attempting to match investments with anticipated cash flow requirements. Unless matched to a specific cash flow, counties should not invest in securities with a maturity date greater than five years. Counties shall adopt average maturity limitations (which often range from ninety days to three years), consistent with investment objectives.

In addition to the interest rate risk measures listed above, counties that pool investments should mitigate **market risk** by setting modified duration ranges and monitor them on a regular basis. Counties that purchase callable securities should also consider effective duration target ranges.

Liquidity risk is managed by having a portion of the portfolio invested in readily available funds such as the LGIP and/or money market account.

Credit risk is managed by regular monitoring of portfolio credit quality, establishing minimum credit rating requirements and maximum sector and issuer requirements.

4. Fair Value Reporting

The market value of all securities in the portfolio should be updated regularly or at least on a quarterly basis from a reputable and independent source. A written report of these values should be disclosed to the governing body or other oversight body at least quarterly. The report should include the market value, book value, and unrealized gain or loss of the securities in the portfolio.

Additionally, pooling counties should make this information available to pool participants on a regular basis and are required as external pools to report on end of year financial statements in accordance with GASB Statement No. 79, www.gasb.org.

5. Using Benchmarks

Measuring portfolio risk and return results against appropriate market benchmarks is a technique to verify all investment objectives are being met and portfolio investment returns are appropriate for the risk incurred.

Portfolio managers should select a benchmark that closely resembles policy constraints and management practice in terms of duration, maturity range, security types, sector allocations and credit quality.

Counties can also assess their investment portfolio for performance and risk by comparing the book, yield and/or total return of the portfolio to carefully selected benchmarks at least quarterly.

6. Accountability and Transparency

An important way for the governing bodies and the public to be informed is through disclosure and reporting. At least quarterly, a report should be submitted to the governing body or other oversight body, prepared in a manner which will allow the participants in the pool to ascertain whether investment activities during the reporting period have conformed to the investment policy. It is also best practice to establish minimum reporting requirements that should be made available, preferably published on a public facing webpage if possible.

7. Using a Third-Party Custodian

State and local governments should utilize independent third-party custodians to safeguard their investments and protect against safekeeping/custodial risks through a competitive RFP process. All securities purchased by the Treasurer (*except for non-eligible items such as non-negotiable CD's, the LGIP, and demand deposit accounts held at qualified public depositaries*) should be held by a third-party custodian and settled on a delivery-versus-payment basis. The Office of the State Treasurer offers a statewide custody program for counties to consider.

8. Relationships with Securities Dealers

A. Selection process
   i. Use a questionnaire, conduct an interview, and conduct peer references to help determine that the broker understands the public entity's needs and objectives.
   ii. A request for proposal process can also be used to acquire information and determine selection of broker services.
   iii. Conduct due diligence on broker/dealers, including registration with FINRA and use FINRA's "Broker Check" tool. Examples on website: http://www.finra.org

B. Monitoring process
   i. Conduct an annual review of broker/dealer sales representatives using FINRA's "Broker Check" tool.
   ii. Review performance which may include trade volume, pricing competitiveness, and product mix available.

C. Conducting investment transactions
   i. Require all Broker/Dealer security transactions settle on a delivery versus payment basis at the entity's custodian bank.
   ii. Retain transaction documentation for audit trail.
   iii. Follow all ethics policies when dealing with broker/dealers.
   iv. Attempt to obtain reasonable market prices on investment transactions.

9. Investment of Bond Proceeds

A. Establish guidelines for permitted investments to preserve capital, maintain liquidity, and achieve a market rate of return.

B. Develop policies and procedures for the investment of bond proceeds that comply with the County's debt policy along with IRS requirements such as arbitrage and competitive pricing rules.

C. Develop policies on the potential use of a municipal advisor or investment advisor and consider using the RFP process to select advisors.

10. Investment Advisors or Consultants

Fiduciary responsibility for the safety and liquidity of government funds cannot be delegated to an investment advisor. Requirements for selection criteria and delegation of authority should be addressed in Investment Policy.

GUIDELINES FOR DEVELOPMENT OF INVESTMENT POLICY

Below is general guidance regarding various elements for investment policies. The policy adopted by each entity will have some variation with those policies adopted by others. The policy should reflect the objectives and constraints of each organization. Every effort should be made by Treasurers, finance officers and approving authorities to understand the philosophy and reasons behind each element of the policy.

1. Policy

The overall policy statement should be a condensed summary of the purpose of the policy. In general, investment policies provide guidelines regarding the objectives of the investment program and define any transferred authority and/or constraints as it relates to the management of the investments.

2. Scope

The scope should clearly define the funds in which the policy applies to and, if applicable, any funds that are excluded from the policy. Considerations should include whether the policy applies to all funds held in the custody of the government jurisdiction and its offices. If certain funds are excluded, provide an explanation of guidance available for the investment/management of those funds.

3. Prudence

Entities should include guidance as to what level of prudence those responsible for making investment decisions will be held accountable. It is best practice to hold all investment professionals to a standard in which they are required to manage the investments with judgement and care, exercising caution to the extent in which they can reasonably mitigate risk. The Prudent Person, as defined in Washington Administrative Code (WAC) 192-100-010, is a standard rule in which is often applied in context of managing the overall portfolio.

4. Objective

The investment policy must contain a concise and clear statement of objectives regarding safety of capital, liquidity and return on investment. Through its statement of objectives, the governing body sets the tone and direction of the policy and the investment program.

Safety of capital is preserved through diversification. Liquidity is protected through matching maturities to anticipated disbursements. Investment Income (return) is the desired outcome of the investment portfolio. A careful balance of achieving safety and liquidity, considering the risk tolerances, should result in additional revenue to the funds in which are being invested.

5. Delegation of Authority

RCW 36.29.020 and 36.29.022 provides authorization for the Treasurer to invest funds not needed for immediate expenditure. The investment policy should contain explicit delegation of authority to specific investment officials responsible for conducting transactions and managing the entity's investment program.

6. Ethics and Conflicts of Interest

Chapter 42.52 of the Washington State RCWs prescribes various ethics standards required for public service employees. Specifically, 42.52.150 covers limitations on gifts. These standards and limitations, along with any specifically prescribed policy or local ordinance should be considered when establishing ethics and conflict of interest standards for investment officials. Guidelines should be established for communicating and/or restricting any business activity that could be construed as a conflict of interest as it relates to financial institutions and/or investment purchases.

7. Authorized Financial Dealers and Institutions

The investment policy should require that a set formal process be used to select and maintain depositories and brokers/dealers. Because the policy is intended to endure, it should not mention specific firms or depositories. The policy should outline any limitations established by state or local law and outline the process in which dealers and institutions are selected.

8. Authorized and Suitable Investments

The selection of investment instruments to be allowed for investment purposes is a significant policy issue for many governments. Although day-to-day selection of specific instruments should be treated as a management function, the policy should define the general universe. From the approving authority's perspective, special care must be taken to ensure that the list of instruments includes only those allowed by law and those in which the investment managers are trained and competent to handle. In selecting authorized investments, consideration should be given to any limitations necessary by issuer, type, maturity as well as required collateralization of applicable instruments.

If repurchase agreements are authorized, prior to execution, a Master Repurchase Agreement must be signed with the bank or dealer.

Credit monitoring should also be a requirement for investments such as corporate notes and municipal bonds.

9. Collateralization

Washington State provides for the collateralization requirements of certificates of deposit with qualified public depositories. The State Treasurer's Office administers the Public Deposit Protection Commission that manages the collateral program for public deposits in qualified public depositories. Statute (Chapter 39.58 RCW) prohibits certificates of deposit with financial institutions that are not qualified public depositaries.

Collateralization requirements for repurchase agreements should be prescribed in this section including types of collateral accepted. The policy should address such points as market valuation responsibility and timing, safekeeping by an independent third party and evidence of ownership.

10. Safekeeping and Custody

The investment policy must include a clause regarding third-party safekeeping and custody of securities and collateral. The policy must also address the delivery of securities, where Delivery Versus Payment (DVP) is a requirement.

11. Diversification

The investment policy should state the purpose of diversification, "to reduce overall portfolio risks while attaining market average rates of return." Diversification should be conceptualized in terms of maturity as well as instrument type and issuer. Thus, the diversification concept in a portfolio should include prohibition against over concentration in a specific maturity sector, as well as constraining the reliance on specific risky instruments and issuers.

12. Maximum Maturities

To protect public funds from market price losses resulting from rising interest rates, the entity may wish to limit the maximum term to maturity on current operating funds' investment to 12 months, the operating budget cycle. Some may find this term unduly restrictive and may employ a two-year (or longer) rule. The latter only appears reasonable if a portion of the assets are not required for expenditure within the one-year budget cycle. The Portfolio's maximum weighted average maturity (WAM) should be no longer than 3 years.

13. Internal Controls

The specific internal control procedures used are beyond the scope of the investment policy and should be a subject of the normal operating procedures of the Treasury. The investment policy should require a system of internal controls. The policy should establish the purpose of the controls in place, preventing control of collusion; separation of duties; reconciliations; and documentation of transactions. The overview may also provide for the timing of periodic reviews and monitoring of controls. The review of internal controls should not be left up to the periodic examination by the Office of the State Auditor, but review of controls is an ongoing responsibility of the entity.

14. Performance Standards

The investment policy should define a formal evaluation of performance and occasional operational audits by defining the benchmark(s) used to determine whether a market rate of return is being achieved by comparison to a benchmark. The benchmark should closely match the structure of your portfolio.

15. Reporting

The policy should establish the minimum reporting requirements. Investment reports provide a mechanism for monitoring by the governing bodies and pool participants of the portfolio. At least quarterly, reports should be submitted to the oversight committee to monitor the impacts of economic conditions, portfolio changes and the results of investment operations. Reporting also provides written communication regarding investment performance, compliance, exposure to investment risk, and a clear representation of the investment portfolio.

16. Investment Policy Adoption

It is best to have the policy certified by an organization recognized by WSACT such as WPTA, Government Investment Officers Association (GIOA), or Association of Public Treasurers (APT). This could be done prior to adoption by the Finance Committee in case changes are recommended by the review panels. The formal adoption of the policy should be adopted by the Finance Committee or governing authority and should be reviewed periodically.

RECOMMENDED INVESTMENT EDUCATION PROGRAM

The mission statement of WSACT states the purpose of our association is to, "provide a forum for all County Treasurers to educate, advocate, mentor and support the creation of effective treasury systems which honor the public trust." Because of the ever-changing complexities of managing public funds, to meet the needs of its members, WSACT will support educational opportunities for its members and staff as it relates to investment management and cashflow forecasting.

The following are general guidelines for suggested training based on two major-investment program groups entities may fall in:

1. Minimum Training Required

To maintain the highest possible professional standards, build skills and remain current on best practices, ethics, and new regulations, counties should provide opportunities and funding for investment personnel to complete continuing education programs or other training in cash and investment management. . The county's investment policy should include minimum hourly training requirements per year based on the responsibility of the position (i.e., Investment Officer, Treasurer, Finance Committee Members). For the Treasurer and investment staff, WSACT recommends a minimum of 24 hours of training every two years in general public fund investing and two hours of ethics.

A. District directed investments or investments only in the State's LGIP
   i. Investment strategies for this group generally include shorter duration targets, however a need for understanding cash flow management and risks associated with various investment vehicles are appropriate.

B. County Treasurers that have pooled investments outside of the State's LGIP
   i. Investment strategies for this group will have varying tolerances for duration targets and liquidity needs. Management of cash flows can be complicated while managing the pooling of funds and require careful analysis of current market conditions, and cash flow patterns.

C. The County Finance Committee consists of the County Treasurer, County Auditor, and Chair of the County Commission/Council (RCW 36.48.070).
   i. This committee is charged with the responsibilities of approving the counties investment & debt policy and "shall make appropriate rules and regulations for the carrying out of the provisions of the RCW(s)…" The focus of this training should be on the elements of a good investment and debt policy and how the finance committee can effectively monitor for compliance with their adopted policies.
   ii. WSACT recommends a new member of the Finance Committee obtain public fund investing training within six months of being appointed.

2. Suggested Training Venues

Recommended trainings can be completed by utilizing educational sessions provided by the following associations/venues: (*See **Appendix A** for links to each of these associations)*

- WSACT
  - Annual Conference
  - District/Regional Training

- Washington Association of County Officials (WACO)
    - Online training library
- WACO/ Washington State Association of Counties (WSAC) Joint Conferences
    - Newly Elected Official Training
- Washington Finance Officers Association (WFOA)
    - Annual Conference
    - Periodic non-conference offerings
- GIOA
    - Annual Conference
    - CGIP Certification program
    - Periodic Webinars
- APT
    - Annual Conference
    - Certified Government Investment Manager training
    - Periodic Webinars
- Government Finance Officers Association (GFOA)
    - Annual Conference
    - Periodic Webinars

3. Monitoring/Compliance:

The WSACT Education Committee will ensure the required investment education classes are offered at the Districts and/or WSACT conferences. Treasurers will be responsible for ensuring any additional required training is obtained. Treasurers will be responsible for monitoring and reporting training for themselves and their investment staff.

Appendix A

WSACT Best Practices Training Resources

Local Associations and Resources:

- Washington State Association of County Treasurers (WSACT)
  - http://countyofficials.org/254/Additional-Resources
- Washington Finance Officers Association (WFOA)
  - https://www.wfoa.org/training-header/
- Washington Public Treasurers Association (WPTA)
  - http://www.wpta.us/conferences.html
- Municipal Research and Services Center (MRSC)
  - https://mrsc.org/Home/Training.aspx

National Associations:

- Government Finance Officers Association (GFOA)
  - https://www.gfoa.org/treasury-and-investment-management-courses
- Government Investment Officers Association (GIOA)
  - https://www.gioa.us/webinars/
- Association of Public Treasurers of United States and Canada (APT)
  - https://www.aptusc.org/

WSACT Best Practice Recommendations for Investing

Policies to govern the County's Investment practices

- MRSC Investment Policies:
  - https://mrsc.org/Home/Explore-Topics/Finance/Finance-Policies/Investment-Policies.aspx
- Guide to Public Funds Investing for Local Governments- Office of the Washington State Treasurer
  - https://www.tre.wa.gov/wp-content/uploads/inv_elig.pdf
- Washington Public Treasurers Association investment policy certification
  - http://www.wpta.us/cert_invest.html
- Government Investment Officers Association Investment policy certification
  - https://www.gioa.us/investment-policy-certification/
- Association of Public Treasurers of United States and Canada investment policy certification
  - https://www.aptusc.org/investment-policy-certification
- Government Finance Officers Association investment policy best practices
  - https://www.gfoa.org/materials/investment-policy

Cash Flow Forecasting

- GFOA: Includes GFOR Using Cash Forecasts for Treasury and Operations Liquidity
  - https://www.gfoa.org/cash-flow-forecasting
- GIOA Webinar: Cashflow Management in the Investment Process: A Practical Approach
  - https://www.gioa.us/files/webinars/GIOA-Cashflow-Webinar-April-26-2021-Hubie-White.pdf

Portfolio Diversification

- GFOA: Diversifying the Investment Portfolio

- https://www.gfoa.org/materials/diversifying-the-investment-portfolio

Fair Value Reporting

- GASB Statement No. 72
  - https://gasb.org/page/PageContent?pageId=/standards-guidance/pronouncements/summary--statement-no-72.html&isStaticPage=true
- GFOA: Mark-to-Market Reporting for Public Investment Portfolios
  - https://www.gfoa.org/materials/mark-to-market-reporting-for-public-investment-portfolios

Using Benchmarks

- GFOA: Using Benchmarks to Assess Portfolio Risk and Return
  - https://www.gfoa.org/materials/using-benchmarks-to-assess-portfolio-risk-and-return
- GIOA Webinar
  - Performance Benchmarking: Book Return and Total Return: The Good, The Bad, and The Ugly- https://www.gioa.us/files/webinars/GIOA_Book_Return_and_Total_Return_Good_Bad_Ugly.pdf

Using a Third-Party Custodian

- https://tre.wa.gov/partners/for-local-governments/statewide-custody-program/
- https://www.gfoa.org/materials/using-safekeeping-and-third-party-custodian-services

Relationships with Security Dealers

- Government Relationships with Security Dealers
  - https://www.gfoa.org/materials/government-relationships-with-securities-dealers

Recommended Certification Programs

- Government Investment Officer Association (GIOA)
  - Certified Government Investment Professional (CGIP) https://www.gioa.us/cgip/
- The Association for Financial Professional (AFP)
  - Certified Treasury Professional (CTP) https://ctpcert.afponline.org/
- CFA Institute
  - Chartered Financial Analysis (CFA) Certification- https://www.cfainstitute.org/en/programs/cfa/charter
- Government Finance Officer Association (GFOA)
  - Certified Public Finance Officer (CPFO) https://www.gfoa.org/cpfo

Additional helpful information

GFOA – Roll of the Finance Officer Best Practices -- https://www.gfoa.org/best-practices/role-of-the-finance-officer

RCW: https://app.leg.wa.gov/rcw/default.aspx?cite=36.29