

**PORT OF SEATTLE**  
**MEMORANDUM**

**COMMISSION AGENDA**  
**ACTION ITEM**

<b>Item No.</b>	<u>6i</u>
<b>Date of Meeting</b>	<u>June 5, 2012</u>

**DATE:** May 29, 2012

**TO:** Tay Yoshitani, Chief Executive Officer

**FROM:** Craig J. Kerr, Treasury Manager

**SUBJECT:** Second Reading and Final Passage of Resolution No. 3663, Restating the Port's Investment Policy

**ACTION REQUESTED:**

Request Second Reading and final passage of Resolution No. 3663: A Resolution of the Port Commission of the Port of Seattle restating the Port of Seattle Statement of Investment Policy; authorizing its implementation by the Treasurer of the Port and Repealing Resolutions No. 3569 and No. 3589 in their entirety.

**SYNOPSIS:**

Staff requests the Commission to authorize an updated Statement of Investment Policy, which includes two updates to better manage the Port's use of Repurchase Agreements, which are short-term investment instruments. The first change is to remove the requirement of executing Repurchase Agreements only with Primary Dealers and allow Port staff to enter into Repurchase Agreements with Port-approved brokers and financial institutions. The second change is to allow Repurchase Agreement Collateral to be extended to the overall maturity limits of the current policy, which is 10 years. All other changes are housekeeping in nature and are intended to strengthen and/or clarify current policy language. These changes do not expose the Port to any additional risk.

**BACKGROUND:**

Best practices in municipal portfolio management include a periodic review and update of the municipality's investment policy. The Port has engaged in policy reviews approximately every four years; the most recent occurred in 2007. In keeping with this practice, staff, working with the Port's Financial Advisor, Seattle Northwest Securities, has undertaken a review of the Port's investment policy and recommends the following changes.

There are two recommended updates to the policy related to Repurchase Agreements.

A Repurchase Agreement is a short-term investment instrument in the form of a collateralized loan agreement between a lender (the Port) and borrower (a dealer) for a set period of time, at an agreed-upon interest rate. The borrower has to collateralize the agreement with securities acceptable to the Port, in compliance with State law and Port policy, and the collateral is held by a third party custodian.

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First, under Section 9-F-2 the policy currently requires that Repurchase Agreement transactions be conducted only with Primary Dealers (security dealers that can buy and sell Government Securities and deal directly with the Federal Reserve Bank of New York). This narrows the universe of bidders since not all Primary Dealers opt to enter into Repurchase Agreements, particularly given the Port's restrictive investment policy. The Port's other dealers, while not "Primary Dealers," are well capitalized, highly liquid and active dealers that can offer competitive rates while providing acceptable collateral with no additional risk to the Port. Staff therefore recommends allowing the Port to enter into Repurchase Agreements with those security dealers and financial institutions on the approved dealer list.

Second, currently in Section 9-F-2 the maturity of underlying collateral for Repurchase Agreements cannot exceed 5 years. Staff recommends extending the collateral maturity to 10 years consistent with the maximum maturity of securities authorized for purchase. (This is separate from the policy limit of 60 days for the agreements themselves). The maximum maturity extension for purchases was approved in 2006 and the intent was to allow collateral to be extended as well; however, the provision was overlooked in the 2006 policy change amendments. In most cases, the collateral the Port receives for repurchase agreements does not exceed 5 years. On occasion, when a Repurchase Agreement exceeds \$50 million, the Port will be offered collateral in several pieces where one piece may exceed 5 years. This complicates the transaction and results in lower interest rates than could be obtained if the longer maturity were allowed. This change affects the underlying collateral only and does not affect the duration of the portfolio.

The remaining changes are administrative in nature. The following is an outline of these "clean-up" changes that parallel with the "red line" draft of Exhibit A to the Resolution.

Change #1 - Section #6 currently reads: "All securities transactions shall be settled on a delivery versus payment (DVP) basis." Staff is requesting the sentence be amended to read "All transactions (involving authorized investments) shall be settled on a delivery versus payment basis." This housekeeping change clarifies the existing language.

Change #2 – A Section Title in Section #8 currently reads "Securities Dealers" Staff is recommending changing the Section title to "Approved Securities Dealers" to better clarify current practice.

Change#3 - Under Section 9-E, staff is correcting the spelling of the word consistent.

Change #4 – In Section 9-F, staff is adding the words "and Annex(es)" to reflect current practice. Any time the Port enters into a Master Repurchase Agreement with a broker or financial institution the Port attaches a copy of its Investment Policy and a document detailing Port staff authorized to execute these transactions. These documents are considered Annex(es) when attached to the Master Repurchase Agreement.

Change #5 – In Section 9-G, staff recommends a change in the language for clarifying the Port's intent with the collateral it furnishes on a Reverse Repurchase Agreement transaction as well as

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making the Approved Security Dealers and Financial Institutions consistent with the recommended change on Repurchase Agreements discussed above.

Change #6 – Section 10 defines the diversification allotment of municipal securities. The Port's Investment Policy has always allowed purchase of municipal securities. However, the policy never contained a defined percentage limit as well as the percentage limit of each issuer the Port is allowed to hold. Staff is recommending changing Port Policy to limit Municipal Securities to 20% of the portfolio and no more than 5% with each issuer.

Change #7 - The footnote in Section 10 describes the action staff must take if an unexpected change in market conditions causes the portfolio to be outside of policy targets. This provision was intended to apply to the violation of any policy limitation, but its placement in Section 10 implies that it applies only to the diversification limitations. Staff is recommending making this footnote its own section for better clarification and monitoring. Therefore, this footnote is now (Section 13 - Policy Exceptions) that would pertain to all policy targets, not just the diversification target, and also include the duration target and maximum maturity limitations.

Change #8 – Adding the language “from settlement date” in Section 11 better defines the Port's 10 year maturity restriction. Ten years from settlement date means that if the Port purchased a security settling on May 1, 2012, the 10 year maturity date period would expire on May 1, 2022.

Change #9 – Section 12 currently reads “2.0 target duration standard...” Staff is recommending adding (2.0 target “modified” duration standard).

Modified duration is calculated to the maturity date of a security and effective duration is calculated to the “call date.” The Port holds callable securities and has always managed its duration to the modified duration target. Managing to modified duration is more conservative and prudent given the nature of the Port's overall portfolio objectives of safety, liquidity and yield.

With the addition of Section 13 explained in Change #7 above the remaining sections have been renumbered.

### **OTHER DOCUMENTS ASSOCIATED WITH THIS REQUEST:**

- Resolution No. 3663
- Copy of the New Exhibit A to the Resolution incorporating all changes set out above.
- “Red Line” copy of Exhibit A to the Resolution

### **PREVIOUS COMMISSION ACTIONS OR BRIEFINGS:**

- December 11, 2001 – Original Investment Policy Approved - Resolution No 3487.
- December 12, 2006 – Policy First Amended - Resolution No 3569.

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- October 23, 2007 – Additional policy amendments adopted- Resolution No 3589.