

The Money Clip



Washington Municipal Treasurer's Association

December 2003

President's Message

Yvonne Ziomkowski, City of Port Angeles

I cannot believe April was eight months ago... I hope all of you had a very productive and enjoyable summer. At this time of the year, I am (like probably the rest of you) up to my eyeballs in the budget process. I have to admit, every year it is more and more difficult to balance the budget.

One of the most enjoyable aspects of my year as President, is the opportunity to represent WMTA with sister organizations in other states and at the APT US & C annual conference. I attended the annual conference for CMTA (California) held in the most beautiful place, Indian Wells (next to Palm Springs), in April/May. I was very impressed with the quality of this conference. I especially enjoyed David Carey talking about "Lessons Learned by a Fighter Pilot". David was a POW for five years in Vietnam. With the war going on, his speech was very timely. He made us cry and laugh. He made us

also realize that there are choices even in the most difficult situation. Never give up!



It was very special for me to meet and listen to Rosario Marin, United States Treasurer at this time. What a wonderful woman! She is further proof that with hard work there is no limit in opportunities. She came to the US from Mexico as a teenager and didn't speak English. But, she worked so hard that she graduated from high school with honors in English! Her story was especially close to my heart.

Other topics included CALPERS, which is the state's defined pension plan. It is one of the largest, if not the largest, in total portfolio size in the US. The major difficulty is funding problems on the public safety side as a result of increased benefits during the late '90s and early 2000s. "Rightsizing, Downsizing, and Capsizing" is as big a problem for Californians as it is for us. One of the solutions is "Collaborative Communication Between Cities, Agencies, Counties, and School Districts." By the way, did you know that City Treasurers

in California are elected? The Finance Director can also run for the Treasurer's position and if elected can collect both salaries.

The APT US & C annual conference was in August in Washington, DC. What a treat! Washington is full of US history, political power, and just beautiful scenery. The Conference provided an excellent educational program. I especially enjoyed the "Treasurer to Treasurer" workshop. What struck me most was how similar we all are. We all struggle with similar problems and issues such as stagnant revenue sources, skyrocketing health care costs, and increased costs of technology mostly as a result of growing customer expectations. Most of us experience budget cuts in spending, but we are still expected to provide more services. Clearly, there is much to be gained by sharing information and cooperating in areas of mutual concern. I hope you don't think we escaped the subject of performance measures; it is still a very high priority issue.

Several economists had very interesting and different outlooks on the economy. Girard Miller, now of Janus Funds, was, as always, interesting and informative. An FBI agent talked about "Fighting the Many Faces of Financial Crimes", Carol Hyatt (author of "When Smart People Fail") and Syble Solomon (founder of LifeWise) gave us strategies for career success and provided us with tools for life planning. I especially enjoyed "Winning Leadership Strategies", a keynote address by Lt. Gen. Norton

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Washington Municipal Treasurer's Association

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A. Schwartz, U.S. Air Force, Director of Operations, and one of the Joint Chiefs of Staff. He stated that every great leader should have these five character counts, situational awareness; credibility; interpersonal skills; values; and ethics. I couldn't agree more and I hope we all incorporate this philosophy in our lives.

For those of us from Washington State, the real highlight of the conference was the presentation of APT US & C Dr. Jackson Phillips Award. Our own State Treasurer, Michael J. Murphy was a recipient of this very prestigious award, which was created in 1980 to recognize one member of the Association annually for his/her leadership in the contribution to management of public funds. The purpose of the award is to encourage innovative programs in municipal governmental finance. I cannot think of anyone who deserves this award more than Mike. *Congratulations!*

I encourage anyone in our profession to be active and involved in professional organizations such as WMTA. It will certainly help your career and you will create a network of great contacts. It always helps me to meet new people, discuss similar work issues, and learn new skills.

I encourage you to take advantage of certification programs provided by the APT US&C and WFOA. An Investment Policy Certification program has been available for several years. Reasonably new is the Debt Policy certification. You will find information about these programs on WMTA web page.

I hope that you still have some training money in your budget. I cannot stress enough how important and beneficial training and networking with peers is! We are already working on next April's conference. This year's theme is "Money makes the world go around." Your educational committee is preparing exciting subjects for the round table discussions and we were lucky to reserve an exciting speaker for the Thursday morning session. We are also making every effort to keep the cost down. Start planning to attend now. It will be in Chelan, April 14 through 16, 2004. Don't forget to start collecting auction items. All auction proceeds support the Scholarship Fund.

As a last thought, I would like to recognize our volunteers and associate members (vendors) who provide so much support to WMTA. Many of them have been active in our organization for years. They provide us with significant financial support, serve as round table facilitators, and assist us with technical topics. Thank you for your support!

Having the opportunity to serve as your president is a great honor for me. I thank each of you as members and those on the board for your support and involvement. ▀



Conference Notes

Arif Kanji, Conference Chair

The 21st annual conference will be held in Chelan, Washington at Campbell's Lodge April 14-16, 2004. The conference theme will be **Money Makes the World Go 'Round**. The keynote speaker will be David Rabiner. His topic on Thursday morning will be How to Succeed, Stay Sane, and Have Fun at Work. A very timely topic.

The conference begins on Wednesday with the golf tournament or for those that are smart enough to stay away from the links and be stress free – Keith Sawdon will be discussing cash flow and banking services including the RFP pro-

cess. Let's see golf, class, golf, class – tough choice here.

The roundtables begin on Thursday with an excellent variety of topics that will be sure to stimulate your thought processes. Entertainment will be provided by the Coats, Thursday night, an excellent a capella singing group. They've been at conference before and we are excited to have them back.

Also keep in mind ideas for the auction. Money raised at this event benefits our scholarship fund, providing opportunities for those folks who

have slim budgets. Education is our main objective and the more people we can reach the better for all.

So plan ahead – we hope to see you all there!▶



WMTA 21st Annual Conference



Construction Financing Adds New Flexibility to LOCAL Real Estate Program

by Michael J. Murphy, Washington State Treasurer

In the realm of the famous Five W's, we until recently were most often asked the "why" question: **Why** don't you offer construction financing?

Well, the answer – and thanks for asking – is, "We do."

The Office of the State Treasurer did its first two construction financings at the May 2003 COP sale. Your jurisdiction can now think in terms of financing construction up front, rather than being reimbursed afterward, as was previously the policy.

We expect this newest wrinkle in our LOCAL program will bring new flexibil-

ity to your decision-making and funding processes.

Here are answers to some other "W" questions:

Why did LOCAL decide to add construction financing to the package?

We have found that most capital projects involve construction, so we are simply meeting a need of local government.

What is the process for getting started?

It's the same process as for buying land and buildings. Submit a Notice of Intent and real estate worksheet by the

cutoff date. Also, submit a credit form if applicable.

What are the approval procedures for our council or commission?

Again, it's the same as with land and buildings or equipment. The council or commission needs to pass an authorizing resolution or ordinance.

When are the deadlines?

They are the same as for land and buildings (please note that real estate financings are now quarterly instead of twice a year).

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The Case for Investment Policies

By Michelle Saddler, Illinois Metropolitan Investment Fund (IMET) (*Reprinted with permission from APT & US&C*)

Introduction

The study of public funds management and, in particular, the investment of public funds, has been evolving and developing since before even the founding of such national associations as the Association of Public Treasurer's and the Government Finance Officers Association. Despite the best of intentions and efforts, losses of public funds have been incurred numerous times throughout the years, and every loss has provided a lesson from which we now can benefit.

The lessons of the 1980s and the lessons of the 1990s have helped government investors develop policies and procedures by which they can safeguard public funds. As the field developed, academicians and practitioners alike repeatedly quoted Will Rogers as saying, "I am more concerned about the return of my principal than the return on my principal."

As we enter the fourth year of the 2000s, and particularly as we once again enter a low-interest, rising-rate environment, we fervently pray that we remember the lessons of the past. It is imperative, therefore, that we review the reasons for having an investment policy in the first place.

Overview

In the 1980s, the public funds market faced the bankruptcy of several broker/dealer firms and of numerous Savings & Loan institutions as well. Unsecured repurchase agreements, not taking delivery of securities, price gouging, and the failure of these trading partners led to significant public losses. The losses galvanized the field and led to the following suggested "remedies:" Appropriate broker/dealer selection and agreements, development and use of Master Repurchase Agreements, use of "Delivery versus Payment," and Competitive Bidding.

In the 1990s, shocking public fund losses resulted from the leveraging of portfolios and using leveraged funds to

invest short-term investment dollars in long-term investments. The result of, and the ensuing remedy for, public funds losses were the use of written investment policies. Such policies ensured that liquidity needs were covered, and they also ensured that government entities would be sold only investment instruments that were suitable for their investment needs as well as for preservation of capital.

Lessons of the 80s

Please note that in the citation of specific government entities that incurred losses, in some cases these are entities that now have established very strong policies and procedures. In several cases, these are entities that now are leading the way in safeguarding the public trust.

In 1982, an agency in the State of New York had invested \$305 million (60 percent of its portfolio) in repurchase agreements with the brokerage firm of Lombard Wall. Lombard Wall had filed for Chapter 11 bankruptcy. The New York agency lost \$21 million after the repurchase agreements were considered merely collateralized loans.

In March 1985, the bankruptcy of ESM Government Securities led to municipal investment losses of approximately \$100 million. Some of these governments had invested in repurchase agreements where they had not taken delivery of the collateral instruments. In other cases, some of these entities had invested in other instruments where they had not taken delivery of their securities: In total, nine government entities in seven different states suffered investment losses, on average, of nearly \$11 million each.

After lengthy disputes and litigation, these municipalities were able to recover only 60 cents on the dollar.

A Bright Spot: Tempe, Arizona, on the other hand, had taken delivery of its investments with ESM, and they suffered

no investment loss at all, nor were their assets held up for any period of time in legal proceedings.

These errors of improper brokerage selection and of not taking delivery took a heavy toll on the field and on the morale of the field in the 80s. Price gouging reported from an Ohio county added to the woes of the time.

Remedies for the Ailments of the 1980s
The lessons of the 1980, consequent to all of the events were:

I) In broker/dealer relations:

- 1) In order to avoid working with uncreditworthy or insolvent trading partners, know the capitalization of your broker/dealer firms. One easy way to ensure adequate capitalization is to work exclusively with Primary Dealers. These are firms that meet the capital adequacy standards of the Federal Reserve Board of New York.
- 2) Verify that the appropriate regulatory bodies in your state license your dealers.
- 3) Check references. Make sure that proposed trading partners have experience in working with governmental customers.
- 4) Diversify among dealers and types of securities.

II) Take delivery of securities and have your own safekeeping agreement. As investment instruments are no longer issued in "bearer" form, investors no longer take physical delivery (as in under your mattress or in your wall safe), but take delivery with your safekeeping bank. Use a safekeeping agreement to ensure ...

III) Use a Master Repurchase Agreement. In the mid-1980s, the Securities and Exchange Commission issued a prototype master Repurchase Agreement. This Master Repurchase Agreement and its

supplemental protections have recently been updated.

- IV) Implement a program of prudent risk control. Such programs may include a formal depository risk policy, credit analysis, and use of full collateralization of public deposits.

Lessons of the 1990s

Unfortunately, once the industry was informed regarding how to avoid less creditworthy trading partners and how to *secure* the investments that they made, there were more lessons to be learned. In the 1990s, new losses stemmed - neither from broker/dealer selection nor from unsecured Master Repurchase Agreements, but losses in the 1990s stemmed from unsuitable investments and leveraging of public funds.

Problems actually began in 1984, when a large California city invested \$750 million of its *cash* in long-term bonds with an average maturity of 17 years. With the cash invested in such long-term securities, liquidity was not available for cash needs. Instead, the City covered its cash needs by *borrowing* against the long-term securities (i.e., by leveraging the funds). The market value of the long bonds declined by more than 10 percent and, when it finally had to liquidate the instruments, the City had lost \$60 million by having to liquidate securities that were “under water,” meaning that they had lost value since their purchase in the amount of \$60 million.

There were other widely publicized debacles as a result of leveraging funds and investing money in unsuitable and risky investment instruments. More than \$2.02 billion was lost by countywide investment pool in Orange County, California subsequent to a 20 percent loss in the value of long-term investment holdings. The County pool borrowed money via reverse repurchase agreements, converting an initial \$7.3 billion into purchase power of \$21.7 billion through use of leverage. The proceeds of these loans were invested in risky, long-term derivative securities.

Losses due to unsuitable investments were not limited to the West Coast,

however. In 1994, the City Colleges of Chicago placed its entire investment portfolio of \$96 million in risky mortgage-backed securities whose value then declined by more than 30 percent. Also in 1994, a local government investment pool in West Virginia became caught in a similar, classic liquidity trap with characteristics as described below.

- The pool employed a speculative investment strategy where the entity was investing in volatile instruments that were highly sensitive to interest rate changes.
- Funds were leveraged, thus putting dollars at risk that did not even belong to the government unit.
- Funds were invested in longer-term securities that lacked the liquidity needed to cover the government’s short-term cash needs.
- No oversight by governing bodies. The treasurers, in many of these cases, were operating without governing body support or appropriate involvement.

Proposed Remedies from the 1990s
The extraordinary magnitude of these losses brought high public visibility to the problem and various professional associations sprang to action proposing mandatory enactment of written investment policies. The mandatory enactment of written policies as espoused by the Association of Public Treasurers, was and still is indented to address the issue of suitability of instruments and maintaining necessary liquidity.

Looking Forward

The Board of Governors of the Federal Reserve Bank eased interest rates in 11 separate easing actions during 2001. Investors watched investment returns continue to decrease throughout 2002, and strong total returns seem nowhere to be found. Added to this is the current, or “recent,” recession in which tax revenues have decreased, and governing bodies are looking for ways to

reduce and to fill budget gaps. In this environment, the temptation to “chase yield” is strong and, as the United States’ economy rebounds during 2003, interest rates will eventually rise, underscoring the market risk of potentially unsuitable long-term investment instruments. As rates rise, long-term bond prices will fall, placing investors in a potential position of loss.

It is critical that public treasurers and finance officials avoid the temptation and the pressure to chase yield. Rather, we must return “back to basics,” as admonished by leaders in key national associations. Governments must ensure that they not only have written investment policies to avoid loss of capital, but they must also ensure that they have complete buy-in from their governing bodies.

These investment policies must include key components addressing, but not limited to:

Scope, objectives, standards of care, safekeeping and custody, suitable and authorized instruments, internal controls, and reporting standards. As units of state and local government review the components of their written investment policies, excellent guidance is available from the APT Model Policy. Although the order of the items as exemplified in the APT Model Policy are important to the flow and to assure comprehensive coverage what is important is that we all remember the lessons of the past, and that we familiarize ourselves with the remedies as prescribed by our forebears and colleagues.

For additional information on developing an investment policy, or for information regarding review and certification of your government’s investment policy, please contact the Association of Public Treasurers Investment Policy Certification Program at www.aptusc.org. ▮

Michelle Saddler is the Executive Director of the Illinois Metropolitan Investment Fund (IMET) in Illinois. She is the former Director of Investments for the State of Illinois and is a former manager in GFOA’s Technical Services Center. Much of the material for this article was originally gathered for *Public Investor* articles written by Kent Rock, Treasurer of Boise, Idaho and President Elect of the Association of Public Treasurers of the U.S. and Canada.

Plan to Attend the 2004 Northwest Clerks and Treasurers Institute

It is time to begin planning to attend the 2004 Northwest Municipal Treasurers Institutes at Seattle University. We have scheduled Treasurers I on July 11, 2004. Early registration is encouraged.

For budget planning purposes, we held the fees and costs down so they are the same as last year. For Treasurers I, the registration fee is still \$395, parking \$30, single room dorm \$195, double dorm room \$130, but the meal ticket for breakfast and lunch remains \$75, and lunch only is \$50. For those who want to stay at a hotel, there is a brand new Silver Cloud Hotel across the street from campus and the Executive Extended Stay Hotel that is two blocks away. The special room rates have not been set for 2004.

Each year, we make a few changes to the course content in order for us to teach the most current practices and to make the classes better. The Treasurers I course offers comprehensive instruction in Treasury Management. On the first day we discuss how the Federal Reserve System and the importance of monetary policies, the creation of money, the banking system and effective cash management. On the second day, we examine investment policies; we visit the City of Seattle Investment operation and the Bank of America trading room, and learn the basics on various investment instruments. We spend the third day on a case study and practical exercises on issuing bonds. In the last two days, we use the computer lab,

learn how to make more effective oral presentations, and discuss ethics and the importance of establishing good internal controls. It is expected that every student will take home and implement at least five good ideas learned in class. Also, we provide a 350 page workbook with articles and other material that can be a helpful resource.

We look forward to seeing you this summer and hope that many of you will work toward completing your Certified Municipal Financial Administrator certification. If you have questions or need a **registration form**, call Lloyd Hara or Liz Anderson (206) 283-9681 or email elizabethanderson4@comcast.net.com.

Your Best Bet for Educational Opportunities *Las Vegas, August 2004*

Mark your calendar to attend the Association of Public Treasurers of US&C (formerly MTA US&C) conference in 2004. Plans are being made for Las Vegas during August 9-12 at the Aladdin Hotel. This is a Monday through Thursday to get the best room rates for our members. The per night rate at the Aladdin is \$109. Airfare on Alaska Airlines from Sea-Tac runs about \$185 to \$225. This is great opportunity for WMTA members to attend a national conference and keep costs down. Beat the odds, register early to take advantage of the best discount early bird prices. These are available until April 1, 2004.

Located midway on the Vegas strip, the Aladdin, rebuilt in 2000, is known for its convenience and luxury. The hotel features gourmet restaurants, shopping and

plenty of entertainment, along with having a health club, spa, business center and pools. The Aladdin is a 10 minute ride from the airport. Las Vegas has become a family destination because of all the things to see and do. Every new hotel try's to out do the last one in having the best tourist draw. There are many restaurants with a wide range of prices.

Work is commencing on the program. Do you base your investments on a roll of the dice or the turn of a card? Are your cash flow predictions like throwing money at the slot machines or hitting it big? How do you adjust to change in the workplace? Do you know when to hold your cards and when to fold? What are the best strategies? There will be some dicey speakers, including Joe

Dervaes, our expert on fraud and recipient of the renowned Cressey Award. Ride the roulette wheel into the world of debt, treasury management, cash handling, collection and disaster preparedness.

State Treasurer Mike Murphy, the 2003 Phillips Award recipient, will be attending to announce the 2004 Phillips Award winner. Let's have the best turn out of Washington delegates that a national conference has seen. The number to beat is 36.

Play your cards right and your participation will make you a winner. Don't gamble away your opportunities for learning when you can have a sure thing by attending the 2004 APT US&C conference in Las Vegas.

2003 Northwest Municipal Treasurers Institute

By Lloyd Hara, Institute Director

Twenty Washington State finance officers attended the Northwest Municipal Treasurers Institute's Treasurers courses at Seattle University this past summer. The introductory Treasurer I course, there were 9 Washington State students. For one week (July 13-18), the students were introduced to the Federal Reserve System, cash management practices, banking services, investments, bond issuance, Internet and technology, internal controls, ethics, oral presentations, and using consultants. A tour of the Bank of America trading room and the Seattle Treasurers Office provides a hands on experience to see what goes on behind the scenes. Much invaluable information is packed into the weeklong sessions.

The following state finance officers attended the 2003 Treasurers I class: Ali Amador (Kenmore), Janet Carr (Snoqualmie), Kathleen Emery (Port Angles), Debra Gore (Ilwaco), Penny Kaech (Mossyrock), Ralph Malone (Okanogan), Tracy Shawa (Pacific County), Caroline Tompson (Port Orchard) and Robert Wagner (Shoreline).

The Treasurer I, 36 hour block of instruction, when combined with an additional 64 hours of instruction offered jointly with the Municipal Clerks Professional Development II and III courses fulfill the educational requirements for the Certified Municipal Finance Administrator program.

Additionally, there were 7 finance officers attending the Professional Development II Course: Julie Breeson (Union Gap), Kay Kammer (Ridgefield), Eden Matlewsky (Blaine), Jenna McDonald (Rosalia), Sherri Sanchez (Blaine), Nickole Schutte (Newport), and Christine Travis (Kahlotus).

Completing their Professional Development III Course were the following 3 finance officers: Wanda Barton Howard (Albion), Nickole Schutte (Newport), and Roger Snell (Lewis County).

Many of the above listed students will meet their educational requirements for certification for the Certified Municipal Finance Administrator (CMFA). The

corps of instructors are persons who have experience in their field and work closely with public officials. There are many opportunities for students to interact and contribute their knowledge with the instructors. It is an opportunity to learn practical applications that can be used when one returns to the office.

The dates for the 2004 Treasurers I Institute are scheduled for July 11-16, 2004. The courses covered will be Monetary Policy and the Federal Reserve, Banking Services and Cash Management practices, Investment Strategies, Bonds and Debt Management, New Technology, Internal Controls, Ethics, and Oral Communications. We plan to hold a session for those who have their CMFA and will concentrate on the electronic office and new technology, protection against fraud and advance investment practices. The registration fee is \$395.

For those persons who desire to attend the 2004 Institute should contact Lloyd Hara at (206) 283-9681. ▀



Construction Financing contined from page 3

Why is construction financing an improvement for the LOCAL program?

It eliminates the need for a local government to pay for construction from its own funds or get a separate loan during construction. It's one-step financing: dollars borrowed up front can be drawn down during construction as needed. We also believe the potential for increased participation in LOCAL will make our rates even more competitive.

Who should we talk to about construction financing?

Call any of the LOCAL staff members listed in this newsletter. We'll be happy to go over the process with you or set up a time to meet. ▀

The Money Clip is a quarterly publication of the Washington Municipal Treasurer's Association. President: Yvonne Ziomkowski; Editor: Rob Hendrickson; Desktop Designer: Holly Martin.

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