

Washington State University

Finance and Administration Investment Policy

I. PURPOSE OF POLICY

The purpose of this investment policy is to set forth the investment and operational guidelines for the management of the financial assets of Washington State University (WSU). These guidelines are designed to ensure the prudent management of financial assets, the availability of operating and capital funds when needed, conformance with state statutes governing the investment of WSU's financial assets, and an investment return competitive with financial market benchmarks. This policy provides the framework of WSU's Office of the Vice President of Finance and Administration within which designated staff's investment activities will operate by setting out objectives, guidelines, and structure. Should bond covenants be more restrictive than this policy, funds shall be invested in full compliance with those restrictions. The Vice President of Finance and Administration reserves the right to amend this policy as deemed necessary.

II. SCOPE

This investment policy applies to all financial assets of Washington State University.

As of the date of the adoption of this policy, the financial assets of WSU include the following portfolios:

Operating Portfolio

These are the operating reserves of WSU and are budgeted to designated areas of WSU. In the absence of external restrictions and internal preferences, all University cash is pooled and invested in the University's Operating Portfolio. The management of these funds on a pooled basis permits greater investment flexibility and provides a larger base from which to meet liquidity demands. All liquidity needs of WSU will be met from these funds.

Dedicated Portfolios

These represent proceeds of bond issues or appropriations for specific purposes that are invested on a short-term basis until needed to fund specific construction projects. Bond proceeds may be invested in one or more dedicated portfolios or in the Operating Portfolio, depending on market conditions, and accounted for individually within WSU's accounting system.

Expendable Gifts Funds

These are gifts of cash donated to WSU to support scholarships, academic, research or capital programs that are available for immediate expenditure and include current use gifts and distributions from endowment. Some may be restricted to a specific purpose, whereas others may be entirely unrestricted.

Included in WSU's financial assets are endowment and quasi-endowment funds. These funds fall under the management guidelines of the Uniform Prudent Management of Institutional Funds Act (RCW 24.55) adopted by the Washington State Legislature in 2009. Under a

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Memorandum of Understanding with Washington State University Foundation, Washington State University Foundation and its Investment Committee have responsibility for the management of these funds. The WSU Foundation Investment Committee has a separate investment policy for the management of endowment and quasi-endowment funds.

III. OBJECTIVES

The objectives of the Office of the Vice President of Finance and Administration's investment activities, in priority order, are safety, liquidity and return on investment.

Safety: Safety of principal is the foremost objective of the investment program. Investing will be undertaken in a manner that seeks to ensure the preservation of capital in the investment portfolios. To obtain this objective, diversification is required in order that losses on individual securities do not exceed the income generated from the remainder of an investment portfolio.

Liquidity: Portfolios will remain sufficiently liquid to enable designated staff to meet all reasonably anticipated cash requirements. This can be accomplished by cash-matching, which is accomplished by structuring the portfolio so that securities mature concurrent with anticipated cash needs or duration matching, which is accomplished by matching the duration of the securities with the duration of the liabilities/withdrawals. Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets.

Return on Investment: Each investment portfolio shall be designed with the objective of attaining a market rate of return through budgetary and economic cycles, considering WSU's statutory investment constraints and cash flow characteristics. Return on investments is of tertiary importance compared to the safety and liquidity objectives described above. The core of investments is limited to relatively low risk securities in anticipation of earning a fair rate of return relative to the risk being assumed.

IV. STANDARDS OF CARE

Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

The standard of prudence to be used by designated staff or designated external investment manager shall be the "**Prudent Person**" standard and shall be applied in the context of managing an overall portfolio under prevailing economic conditions at the moment of investment commitments. Designated staff of designated external investment manager acting in accordance with written procedures and the investment policy and exercising due diligence, shall be relieved of personal responsibility for an individual security's credit risk

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or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments.

The determination of whether a designated staff or designated external investment manager has exercised prudence with respect to an investment decision, shall take into consideration the investment of all funds over which the official had responsibility rather than a consideration as to the prudence of a single investment, and, whether the investment decision was consistent with the written investment policy of the entity.

V. DELEGATION OF RESPONSIBILITIES

- A. The Office of the Vice President of Finance and Administration retains external investment managers to provide day-to-day portfolio management of the public funds. External investment managers are selected based on their experience in public funds management, adequacy of staff, compatibility of investment philosophy with that of WSU, past investment results, and ability to provide competent and timely economic assessments and investment advice. Investment managers must be registered with the Securities and Exchange Commission as registered investment advisers unless specifically excluded from registration (e.g. banks). Managers have full discretionary authority with respect to the assets assigned to them, subject to the guidelines and standards specified in this investment policy.
- B. WSU participates in the Office of State Treasurer's Statewide Custody program for safekeeping of investments to protect against the loss of public funds arising from negligence, theft, or misuse. Custodial services include safekeeping of securities, timely collection of income and other inflows, timely settlement of purchases and sales, disbursements as directed by authorized WSU staff and monthly accounting of all transactions and security holdings.
- C. The Office of the Vice President of Finance and Administration's Treasury staff is responsible for maintaining adequate cash balances in WSU's main checking accounts and for transferring cash more than immediate needs to the appropriate external investment managers. Treasury staff coordinate additions to and withdrawals from investment portfolios with the external investment managers and the asset custodian. Authority for requesting portfolio withdrawals has been delegated to the AVP for Financial Services and the Senior Investment Manager.

VI. ETHICS AND CONFLICTS OF INTEREST

- A. The Office of the Vice President of Finance and Administration recognizes that the investment portfolios are subject to public review and evaluation. The overall program will be designed and managed with a degree of professionalism that is worthy of the public trust.

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- B. WSU Officers and staff involved in the investment process shall refrain from personal business activity that may conflict with the proper execution of the investment program or may impair their ability to make impartial investment decisions.

- C. All persons responsible for investment decisions or who are involved in the management of WSU assets shall be governed in their professional investment activities by the code of conduct established by the applicable state statutes, the Securities and Exchange Commission and the Standards of Professional Conduct of the CFA Institute.

VII. AUTHORIZED INVESTMENTS

Operating Portfolio/Dedicated Bond Portfolios

Eligible investments are only those securities and deposits authorized for public funds in the State of Washington as prescribed in the following statutes: RCW 39.58.130, RCW 43.84.080, RCW 43.250.040 and RCW 28B.10.928. Eligible investments include:

- (1) Obligations of the U.S. government (RCW 43.84.080), (RCW 28B.10.928);
- (2) Obligations of U.S. government agencies or of any corporation wholly owned by the U.S. government (RCW 43.84.080), (RCW 28B.10.928);
- (3) State, county, municipal or school district bonds, note, or in warrants of taxing districts of the State of Washington, provided they are within the limit of indebtedness prescribed by law for the issuing taxing district and are general obligations (RCW 43.84.080);
- (4) Federal home loan bank notes and bonds, federal land bank bonds and federal national mortgage association notes, debentures and guaranteed certificates of participation, or the obligations of any other government sponsored corporation whose obligations are or may become eligible as collateral for advances to member banks as determined by the board of governors of the federal reserve system. (RCW 43.84.080), (RCW 28B.10.928);
- (5) Banker's acceptances purchased on the secondary market; (RCW 43.84.080), (RCW 28B.10.928);
- (6) Investment deposits as defined in RCW 39.58.010 (9) with financial institutions qualified by the Washington Public Deposit Protection Commission (RCW 39.58.130);
- (7) Commercial paper purchased on the secondary market, provided that such commercial paper adheres to the investment policies and procedures adopted by the state investment board as outlined in Section VIII of this policy (RCW 43.84.080), (RCW 28B.10.928);
- (8) State, county, municipal or school district bonds, notes, or warrants of taxing districts of the State of Washington, provided they are within the limit of indebtedness prescribed by law for the issuing taxing district and are general obligations;(RCW 43.84.080)
- (9) Bonds of the State of Washington and any local government in the State of Washington, provided they have, at the time of investment, one of the three

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- highest credit ratings of a nationally recognized rating agency; (RCW 28B.10.928);
- (10) General obligation bonds of any state other than the State of Washington and general obligation bonds of any local government of a state other than the State of Washington, which bonds have, at the time of investment, one of the three highest credit ratings of a nationally recognized rating agency (RCW 43.84.080), (RCW 28B.10.928);
 - (11) Corporate notes purchased on the secondary market, if they adhere to the investment policies and procedures adopted by the state investment board as outline in Section VIII of this policy (RCW 43.84.080), (RCW 28B.10.928);
 - (12) Office of State Treasurer Local Government Investment Poole (LGIP) (RCW43.250.040)
 - (13) Registered warrants of a local government in Whitman County, subject to compliance with RCW 39.56.030; (RCW 28B.10.928);
 - (14) United States dollar denominated bonds, notes, or other obligations that are issued or guaranteed by supranational institutions, provided that at the time of investment, the institution has the United States government as its largest shareholder (RCW 28B.10.928);
 - (15) Repurchase agreements and reverse repurchase agreements, subject to the guidelines outlined in Section VIII of this policy.

Expendable Gifts Funds

Management and investment of donated/gift funds are prescribed in the following statutes: RCW 28B.30.150 and RCW 24.55.015.

- (1) The Board of Regents of WSU have the authority to accept gifts and to adopt proper rules to govern and protect the gift proceeds and income thereon. (RCW 28B.30.150 (24));
- (2) An institution may invest in any kind of property or type of investment consistent with RCW 24.55.015 (RCW 24.00.015 (c)).

VIII. INVESTMENT PARAMETERS

- A. Commercial paper is subject to the following guidelines, in accordance with WSIB Policy Number 2.05.500:
 - a. Rated with the highest short-term credit rating category of any two major Nationally Recognized Statistical Ratings Organizations (NRSROs), at the time of purchase;
 - b. Rated with the highest rating from all the organizations if rated by more than two major NRSROs;
 - c. Holdings may not have maturities exceeding 270 days;
 - d. Any paper purchased with a maturity longer than 100 days must also have an underlying long term senior unsecured credit rating in one of the three highest rating categories of an NRSRO, at the time of purchase;
 - e. Holdings of any single issuer will not exceed 3% of the total assets of any portfolio;

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- f. The percentage of commercial paper will not exceed 25% of the total assets of the total portfolio;
 - g. Must be purchased in the secondary market and not directly from the issuers.
 - B. Investment in corporate notes are subject to the following guidelines, in accordance with WSIB Policy Number 2.05.500:
 - a. Corporate notes are defined as debt securities issued by corporations.
 - b. Corporate notes must be rated at least weak single-A or better by all the major rating agencies that rate the note at the time of purchase.
 - c. The maturity of the corporate notes shall be 5.5 years or less at the time of purchase.
 - d. The maximum duration of the corporate note segment of the total portfolio shall not exceed 3 years.
 - e. No corporate fixed-income issue may exceed 3 percent of the cost or 6 percent of the market value of the assets of the total portfolio.
 - f. The percentage of corporate notes that may be purchased from any single issuer rated AA or better by all major rating agencies that rate the note is 3 percent of the assets of the total portfolio.
 - g. The percentage of corporate notes that may be purchased from any single issuer rated in the broad single-A category from all the major rating agencies that rate the security, is 2 percent of the total portfolio.
 - h. Corporate notes must be purchased on the secondary market and not directly from the issuers.
 - i. Securities rated in the broad single-A category with a negative outlook may not be purchased. Portfolio holdings of corporate notes downgraded to below single A and portfolio holdings of securities rated single A with their outlooks changed to negative may continue to be held, but no additional purchases are permitted.
- C. The commercial paper and corporate notes together are known as the credit portfolio, and is subject to the following guidelines, in accordance with WSIB Policy Number 2.05.500:
 - a. The credit portfolio shall not exceed 25 percent by market value of all assets of the total portfolio.
 - b. The credit portfolio must be diversified by sector and industry.
 - c. Portfolio managers must routinely monitor the ratings and credit quality of the issuers of the commercial paper and corporate notes that they are purchasing. Appropriate personnel should be notified of any credit rating downgrades of issuers in the credit portfolio.
- D. The total portfolio, which includes all money market and fixed income securities in the portfolio are subject to the following guidelines, in accordance with WSIB Policy Number 2.05.500:
 - a. The following are not permissible investments: Loans, derivatives, and securities issued in currencies other than the U.S. dollar.
 - b. No single credit issuer shall exceed 3 percent of the total portfolio's market value.
 - c. The individual country limit of non-U.S. and non-Canadian exposure is 2 percent of the total portfolio. Exposure is determined by the country of domicile of the issuers of portfolio securities.

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- E. Repurchase and reverse repurchase agreements will be subject to the following restrictions:
- a. Transactions will be conducted only with primary dealers, the University's bank of record, or University custodial bank;
 - b. Purchased securities used in repurchase agreements will be limited to government securities;
 - c. Agreements with any single primary dealer or financial institution will not exceed 20% of the portfolio;
 - d. The maximum term of any repurchase agreement is 180 days;
 - e. The share of the portfolio allocated to repurchase agreements with maturities beyond 30 days will not exceed 30% of the total portfolio;
 - f. The maximum term of reverse repurchase agreements will be 180 days and must be matched to anticipated cash flow adequate to liquidate the transaction;
 - g. The maximum portion of the portfolio allocated to reverse repurchase agreements will not exceed 30% of the total portfolio.
 - h. Only securities authorized in statute for the investment of public funds may be accepted as collateral;
 - i. Market value, plus accrued income, of securities used as collateral in a repurchase agreement must be at least 102% of the value of the agreement, plus accrued income.

IX. INTERNAL CONTROL

The Office of Finance and Administration maintains internal controls to protect against the loss of public funds arising from negligence, theft, or misuse. These controls include:

- Use of third-party custody and safekeeping.
- Clear and written delegation of investment authority.
- Avoidance of physical delivery of securities.
- Written confirmation of transactions for investments and wire transfers.
- Written wire transfer agreement with third-party custodian.

X. INVESTMENT OBJECTIVES/PERFORMANCE STANDARDS

Investment portfolios will be managed in accordance with the parameters specified within this policy. Investment portfolios will be designed to obtain an average rate of return during budgetary and economic cycles, consistent with the investment objectives and cash flow needs. A series of appropriate benchmarks shall be established against which performance shall be compared on a regular basis. The benchmark will be reflective of the actual securities being purchased and the risks undertaken. The benchmarks will have a similar weighted average maturity or duration (as appropriate) as the portfolio being measured.

A. Operating Portfolio

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- a. Objective: The primary investment objectives of this portfolio are preservation of principal and liquidity; income is a secondary objective.
- b. Risk tolerance: Realized losses are not desirable, but can be tolerated if it is part of the strategy to produce higher income overall in the portfolio. Financial (credit) risk is not acceptable. Because of the short investment horizon (the portfolio has a 1.2-year modified duration), exposure to interest rate risk and purchasing power risk will be minimal.
- c. Rate of return: The annual time-weighted rate of return of this portfolio should exceed the annual total return of the benchmark, which is 40% Bank of America Merrill Lynch 3-Month U.S. Treasury Bill Index/ 60% Bank of America Merrill Lynch 1 to 3 Year U.S. Treasury Index, after taking into consideration the payment of investment management fees.

B. Dedicated Portfolio

- a. Objective. The primary investment objective of this type of portfolio is preservation of principal and sufficient liquidity to meet funding of expenses incurred during the project. Income is a secondary objective. When market conditions permit, the investments are structured to provide a cash match to the anticipated construction spending schedule.
- b. Risk tolerance. Some principal volatility is tolerated, but enough of the fund will be invested in nonvolatile, liquid investments to ensure payment for projects when due. Financial risk is not acceptable, and because the investment time horizon is less than two years, exposure to interest rate risk and purchasing power risk will be minimal.
- c. Rate of return. The annual time-weighted rate of return of this portfolio should exceed the total return on six-month Treasury bills, after taking into consideration the payment of investment management fees.

C. Expendable Gift Funds

- a. Objective. The primary investment objective of this type of portfolio is preservation of principal and sufficient liquidity to meet funding of expenses incurred during the project. Income is a secondary objective. Investment income is posted centrally and not to the individual underlying gifts.
- b. Risk tolerance. Some volatility of principal is acceptable to obtain additional income. Financial risk is not acceptable, and interest rate risk and purchasing power risk will be minimal, given the investment horizon.
- c. Rate of return. The annual time-weighted rate of return of this portfolio should exceed the total return on the Bank of America Merrill Lynch 1 to 3 Year U.S. Treasury Index, measured over rolling three- and five-year periods, after taking into consideration the payment of investment management fees.

XI. REPORTING

Reports will be provided as requested by the Vice President of Finance and Administration.