Working Capital Investment Guidelines

Office of Budget and Finance
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1. **INTRODUCTION**

   Currently, CUNY and its Colleges have Working Capital cash as part of normal operations. Working Capital is required to ensure that CUNY and the Colleges are able to continue their operations and have the capacity to cover current and future expenses. Working Capital cash flows lead to recurring cash balances which the Colleges typically invest in money market and certificate of deposit accounts that have little to no yields. Getting better returns typically requires either reducing liquidity or increasing investment risk, or both. The University must also be able invest operating reserve funds that are held to meet unexpected needs while conforming with applicable federal, New York State, New York City and CUNY requirements.

   Colleges should perform projections of their inflows and outflows of cash to determine where opportunities may exist to invest Working Capital. Working Capital must be invested only in the types of securities listed in these guidelines, unless an exception is granted.

2. **PURPOSE**

   These guidelines articulate the requirements and investment guidelines related to Tier 1 (short-term cash) and Tier 2 (intermediate-term investments). The primary objectives of the Working Capital guidelines are to: (1) set investment parameters, (2) establish limits consistent with the College and University’s liquidity needs, and (3) define risk tolerance. Investment activities shall be guided by the objectives of safety, liquidity and yield. Specifically the objectives include:

   - To adequately safeguard principal (safety);
   - To maintain and provide adequate cash flow to meet all operational requirements (liquidity); and
   - To obtain a reasonable rate of return (yield).

3. **SCOPE**

   Unless otherwise specified, these guidelines apply to all Colleges, as that term is defined below. These guidelines do not apply to college foundations or separately-incorporated alumni associations; however, those entities are strongly encouraged to establish Working Capital policies of similar scope to maximize the return of funds while maintaining safety and liquidity. These guidelines are recommended as best practice for the College’s auxiliary enterprise corporations.

4. **DEFINITIONS**

   As used in this guideline:

   “College” means a constituent unit of the University, including without limitation senior and community colleges, graduate and professional schools, Macaulay Honors College and the central office, as well as fund groups and organizations that are not legally separate from the University (e.g., the Queens College Athletic and Recreational Fund, the college associations of Hunter College, the School of Professional Studies and the Graduate School of Public Health and Health Policy). For purposes of this Guideline, “college” also includes the Related Entities, unless otherwise indicate.
“CUNY” and “University” mean The City University of New York.

“Federal Deposit Insurance Corporation (FDIC)” is an independent agency created by the Congress to maintain stability and public confidence in the nation’s financial system. “FDIC insurance” protects deposits in the unlikely event of a bank failure. The standard insurance amount is $250,000 per depositor, per insured bank, for each account ownership category.

“Related Entities” means the following types of entities and their subsidiaries, if legally separate from the University and unless otherwise indicated: auxiliary enterprise corporations, college associations, student services corporations, childcare centers, performing arts centers, and art galleries.

“SEC” means the U.S. Securities and Exchange Commission.

“Working Capital” is the pool of resources available from a College’s operations to meet the College’s financial obligations.

5. AUTHORIZED INVESTMENT ASSET GUIDELINES

**Tier 1: Short Term Cash Portfolio**

The short-term cash portfolio provides a high level of liquidity for operating needs and anticipated near-term cash requirements. The objectives of the portfolio are to preserve the principal value, meet the liquidity needs, and earn a return consistent with these guidelines and market conditions. Safety and liquidity are the two primary objectives for this Tier. The average weighted maturity of the portfolio may not exceed one year. The following fixed-income instruments and cash securities are approved for investment to support short-term cash needs:

- **U.S. Treasury Obligations**: Bills, Treasury Inflation-Protected Securities (TIPS), Notes and any other obligations or securities issued by or backed by the full faith and credit of the United States Treasury.
- **Federal Agency Obligations**: Bonds, Notes and other obligations of the United States, and securities issued by any federal government agency or instrumentality or government-sponsored enterprise that has a rating no less than the rating on U.S. Government debt. Collateralized mortgage obligations should not be purchased.
- **Municipal securities**: Taxable and tax-free commercial paper, variable rate demand notes, pre-refunded municipals, synthetic floaters, auction rates securities, bonds, and notes.
- **Commercial paper**: Asset Backed CP, USD Denominated Euro CP, Extendable Commercial Notes, and corporate notes and bonds of domestic corporations.
- **Certificate of deposits** (Domestic, Eurodollar and Yankee): Eurodollar deposits, Time deposits, Deposit Notes, Bank Notes, and Banker Acceptance issued by any commercial banks with equity equal or greater than $1 billion.
- **Certificates of deposit**: with commercial banks with equity below $1 billion if the deposit qualifies for FDIC insurance.
• **Repurchase or reverse repurchase agreements**: collateralized 102% by U.S. Treasury or U.S. Government Agency Obligations.

• **Money Market Mutual Funds**

• **Additional Products**, which includes *Money Market* and Federally Insured Cash Accounts.

**Tier 2: Short to Intermediate Term Portfolio**

The Tier 2 short to intermediate term portfolio represents Working Capital funds that do not need to be readily available to meet operating needs, but represent operating reserves that may be required to fund unexpected needs or strategic initiatives. The average weighted maturity of the portfolio may not exceed 5 years. Safety and Yield are the two primary objectives for this Tier. The objectives can be achieved through investments in a professionally-managed diversified portfolio consisting primarily of U.S. fixed-income securities. The following are eligible instruments:

- All eligible investments permitted in Tier 1.
- **Repurchase and reverse repurchase agreements** collateralized by eligible investments in Tier 1.
- **Asset-Backed Securities (ABS)**: mortgage-backed securities including residential and commercial assets (RMBS and CMBS).
- **High Grade Corporate Debt**
- 10% +/- 5% of the portfolio can be invested in Tier 3 to enhance yield.

**Tier 3: Long Term Portfolio**

Tier 3 represents long-term Working Capital funds that are available for investment for periods greater than 5 years and should be invested in a diversified portfolio that follow the *University's Investment Policy*, such as CUNY’s Long-Term Investment Pool. The primary objective in this Tier is to maximize long-term real return commensurate with risk tolerance of the University. The University’s Investment Policy governs Tier 3 and supersedes the limits set forth in these guidelines policy for asset allocation and issuer limitations.

Colleges and related entities who have Tier 3 investment opportunities are encouraged but not required to invest in the University’s Long-Term Investment Pool.

6. **GENERAL RISKS MITIGATION**

The below section outlines the requirements for mitigating risk in Tier 1 and Tier 2 investments. The University's Long-Term Investment Policy, which is considered Tier 3, addresses risk within these same categories.

**A. Custodial Credit Risk**

Custodial credit risk is the risk that, in the event of a failure of the counterparty, the University will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the College or University and are held
by either the counterparty or the counterparty’s trust department or agent, but not in the College or University’s name.

The College Business Office for a College or the University Treasurer Office for the central office shall mitigate this risk by completing an annual review of the custodian bank and their credit rating. The College or University will not take physical possession of investment securities. All investment securities shall be registered in the name of the College or University.

B. Credit Risk
Credit risk is the risk of loss due to a debtor’s non-payment of a fixed-income instrument (either the principal or interest (coupon) or both). These risks are mitigated by investing in highly-rated debt. Security ratings are based on the ratings provided by one of the three major rating agencies: S&P Global Ratings (“S&P), Moody’s Investors Service (“Moody’s), or Fitch Ratings (“Fitch”). The securities invested in must meet the following criteria:

Tier 1
I. Municipal obligations rated A-1 or higher by a nationally recognized rating agency.
II. Certificates of Deposit, Time Deposits and Bank Notes of domestic banks and domestic offices of foreign banks with a rating of at least A-1 by S&P and P-1 by Moody’s, for maturities of one year or less, and a rating of at least AA by S&P and Aa by Moody’s, for maturities over one year.
III. High Grade Commercial Paper and Banker Acceptance - must have the highest rating (A1/P1/F1) from one of the nationally-recognized rating organizations.
IV. Money market funds or short duration fixed-income funds that are regulated by the SEC and carry an overall average quality rating of A or better.
V. For funds or commingled vehicles that are not rated, these guidelines permit investment in such funds if they generally comply with the eligible investment list in these guidelines.

Tier 2
All individual securities at the time of purchase must be of investment-grade quality. All issuers must have a minimum short-term ratings of A-2 by S&P or P-2 by Moody’s, or long term ratings of BBB by S&P or Baa2 by Moody’s.

The issuing corporations must have a rating of P-1 or better by Moody’s or A-1 or better by S&P or an equivalent rating by Fitch. If the rating is supported by a bank letter of credit, the letter of credit must be issued by a bank having a minimum credit rating consistent with the above.

Asset-backed and mortgage-backed securities must be rated at least A- or higher by one of the major rating agencies at the time of purchase.

C. Concentration of Credit Risk
Investments should be diversified by issuer. The purpose of credit diversification is to minimize unsystematic risk and to provide reasonable assurance that no single security or class of securities will have a disproportionate impact on the portfolio. No more than 5% of the portfolio may be invested in debt obligations of any one issuer (as defined by the ultimate parent company), except the following:
I. Up to 100% of the portfolio may be invested in obligations of the U.S. Treasury.
II. Up to 50% of the portfolio may be invested in money market mutual funds regulated under SEC rule 2a-7. Investments in money market mutual funds should not exceed 10% of the vehicle total net assets.

III. Up to 33% of the portfolio may be invested in obligations of any one U.S. government agency or municipal securities.

IV. Up to 25% of the portfolio may be invested in repurchase agreements.

V. Up to 50% combined exposure to ABS/RMBS/CMBS in Tier 2

D. Counterparty
Counterparty risk is the likelihood or probability that one of those involved in a transaction might default on its contractual obligation. All financial institutions with which the University conducts business with must be credit worthy.

a) Depository banks must be rated BAUERS 4 star or above.

b) Broker/Dealers must be:
   - Primary dealers and regional dealers that qualify under SEC rule 15c3-1 (uniform net capital rule);
   - Capital of at least $50 million;
   - Registered as a dealer under the Securities Exchange Act of 1934;
   - Member of FINRA;
   - Registered to sell securities in New York State;
   - Engaged in the business of effecting transactions in U.S. government agency obligations for at least five consecutive years; and
   - Security dealers not affiliated with a bank shall be required to be classified as a reporting dealer affiliated with the New York Federal Reserve Bank, as primary dealers.

c) Investment institutions must be:
   - Registered as an Investment Adviser with the SEC under the federal Investment Advisers Act of 1940;
   - Have at least five (5) years of experience in providing investment management services; and
   - Registered to do business in the State of New York.

E. Interest rate risk
The University invests in a diversified portfolio comprised of assets that respond differently to changes in interest rates in order to mitigate market fluctuations. The Tier 1 portfolio shall have an average maximum maturity of 1 year or less.

F. Foreign Currency
Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. To address foreign exchange exposure, all investments in a Tier 1 short-term cash portfolio and in a Tier 2 short to intermediate term portfolio must be denominated in U.S. dollars.
7. GENERAL GUIDELINES

- Repurchase agreements must be fully collateralized (including collateral for accrued interest) by any of the securities approved under these guidelines. The current market value of the collateral must cover the principal amount of the investment at all times during the term of the investment.
- The composition of any commingled fund, separate account, or other diversified investment vehicle must meet the criteria for approved securities.
- Downgrade guidelines: At time of purchase, all investments shall conform to the credit-rating requirements of these guidelines. Any subsequent downgrade in credit rating after the time of purchase will not constitute a violation of this requirement. However, securities which are downgraded below minimum acceptable rating levels must be promptly reviewed and a plan of action should be determined within a reasonable amount of time.
- The portfolio may purchase securities on a when-issued basis or for forward delivery. Forward delivery trades cannot exceed the maximum maturity from trade date.
- Non-rated individual securities must be insured or enhanced to the extent that the credit requirements of these guidelines are met. Unrated securities are also permissible if deemed to meet the rating criteria of “pari passu” rating. A pari passu rating is based on the rating of other securities issued by the same issuer or of the issuer itself.
- Split rated credits with two ratings will be considered to have the lower rating. In the event a security has three ratings the majority rating will apply.
- The use of derivative, leverage and/or speculative trading is prohibited.

8. FRAUD REPORTING PROCEDURES

Colleges shall follow CUNY’s breach reporting procedures in the event of any alleged fraudulent or criminal activity:

- CUNY’s 2020 Protocol for Reporting Allegations of Corruption, Fraud, Criminal Activity, Conflicts of Interest or Abuse
- Breach of Private Information Procedure

9. INTERNAL CONTROLS

General Requirement:

- All participants in the investment process shall seek to act responsible and shall avoid any transaction or perception that might impair independence.
- Investments shall at all times be made with judgement and care, under circumstances then prevailing, that persons of prudence, discretion and intelligence exercise in the management of their own funds, not for speculation, but for investment, considering the safety of the principal as well as the probable income to be derived.
- College and University officers and employees involved in the investment process shall refrain from personal business activity that could impair their ability to make impartial investment decisions on behalf of the College or University.

The following internal controls must be enforced:

- The separation of transaction authority from accounting and record keeping authority.
• The separation of wire transfers and investment transaction duties. Wire transfers must be performed by a party outside the investment management process.
• All physical deliveries or book entries of principal and/or interest shall be performed by a third-party custodian.

When the size of a College’s business office does not allow for proper segregation of duties between two or more individuals, then the University’s Office of Internal Audit will provide assistance in the establishment of compensating internal controls such as increased monitoring. These compensating controls shall be documented in writing and approved by the college’s Vice President of Finance, University Executive Treasurer and University Director of Internal Audit.

10. RECORDS RETENTION
Colleges shall follow the University’s Records Retention and Disposition Schedule with respect to the maintenance of Working Capital and investment records.

11. GUIDELINES IMPLEMENTATION AND ADMENDMENTS
The University Office of Budget and Finance is responsible for the periodic review and updates to these guidelines, as well as for ensuring that all appropriate parties are informed of it.

12. HELPFUL RESOURCES
CUNY Banking Policy: http://www.cuny.edu/bankingpolicy
CUNY Cash Accountability Policy: http://www.cuny.edu/cashaccountabilitypolicy
CUNY Investment Policy: http://www.cuny.edu/investmentpolicy
Record Retention Schedule: https://policy.cuny.edu/schedule/
Financial Industry Regulatory Authority (FINRA): https://www.finra.org

13. EFFECTIVE DATE AND TRANSITION
These guidelines are effective beginning on September 1, 2021.