

**LOCAL FINANCE NOTICE**CHRISTINE TODD WHITMAN  
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DIRECTOR**Local Government Investments and Cash Management Plans**

State law concerning investment of local government unit funds was recently amended when Chapter 148, P.L. 1997, was signed into law by Governor Whitman on June 30, 1997. This new act is the first significant reform to local government investment and cash management policy in many years. Chapter 148 eliminates obsolete language and codifies many traditional practices. It also revises and expands the responsibility of the governing body and the role of the Chief Financial Officer in cash management. The 1991 language that permits investment in government mutual funds, purchased through banks, was modified to allow government money market mutual funds to be purchased through registered broker/dealers and banks.

Local officials should carefully review this new law to see how it affects them and what new cash management options it allows. The Division of Local Government Services is working to develop model cash management plans and policies that can be adopted for January 1998. We anticipate continuing education seminars on the new law will be held in the near future. A copy of the law is enclosed for your convenience. This Notice is broken down into eight sections:

- A. General Authority
- B. Permitted Investments
- C. General Investment Practices
- D. Special Conditions on Certain Investments
- E. Cash Management Plans and Policies
- F. Use of Investment Advisors
- G. Investments and Risk
- H. Other Concerns.

Chief financial officers should share this Notice with their governing bodies and other appropriate officials. Investment provisions also affect boards of education.

***A. General Authority***

Local units that must invest and deposit funds pursuant to a cash management plan adopted by the governing body include those that fall under the provisions of the Local Fiscal Affairs Law (N.J.S.A. 40A:5-1 et seq.). Generally, this includes municipalities, counties, authorities, fire districts, joint insurance funds, library boards, and joint meetings. When New Jersey banks are referred to in the law, it means those approved by the Department of Banking and Insurance under the Government Unit Depository Protection Act (GUDPA). Deposits of public funds in banks other than those in the GUDPA program are prohibited by law.

***B. Permitted Investments***

N.J.S.A. 40A:5-15.1(a)

The law modified the investments that are permitted for local government units. Amendments to N.J.S.A. 40A:5-15.1(a), (hereafter referred to as 15.1(a)) also clarified several existing practices; elaborated on several others; and, created new options. The options in 15.1(a) now include the following vehicles:

- Bonds or other obligations of the United States of America or obligations guaranteed by the United States of America. This includes instruments such as Treasury bills, notes, and bonds.
- Government money market mutual funds.
- Any federal agency or instrumentality obligation authorized by Congress that matures within 397 days from the date of purchase, and has a fixed rate of interest not dependent on any index or external factors. This eliminates derivatives, indexed rate, or rate reset obligations.
- Bonds or other obligations of the local unit or school districts of which the local unit is a part.
- Any other obligations with maturities not exceeding 397 days, as permitted by the Division of Investments.
- Local government investment pools, such as New Jersey CLASS, and the New Jersey Arbitrage Rebate Management Program.
- New Jersey State Cash Management Fund
- Repurchase agreements (repos) of fully collateralized securities, subject to conditions discussed in detail below.

In addition, a variety of State laws permit local governments to invest a wide range of obligations issued by State government and its agencies. Appendix A provides detail of the meaning of bonds or other obligations of the United States and federal agencies and instrumentalities.

***C. General Investment Practices***

N.J.S.A. 40A:5-15.1(b through d)

The law also recognized the increasing sophistication of public sector money management by specifying several practices for local government units. The following requirements affect all local units:

- Any investment instruments in which the security is not physically held by the local unit shall be covered by a third party custodial agreement, which shall provide for the designation of such investments in the name of the local unit and prevent unauthorized use of such investments. *15.1(b)*
- Purchase of investment securities shall be executed by the "delivery versus payment" method to ensure that securities are either received by the local unit or a third party custodian prior to or upon the release of the local unit's funds. *15.1(c)*

- Any investments not purchased and redeemed directly from the issuer, government money market mutual fund, local government investment pool, or the State of New Jersey Cash Management Fund, shall be purchased and redeemed through the use of a national or state bank located within this State (GUDPA approved) or through a broker-dealer. In this case, a "broker-dealer" is a securities broker-dealer registered with the New Jersey Bureau of Securities. 15.1(d)

The act also formally exempts banking services and investment purchases from the bidding provisions of the Local Public Contracts Law. Hiring of investment advisors is still subject to requirements of hiring professionals.

#### *D. Special Conditions on Certain Investments*

The law also established a series of special criteria for government money market funds, repurchase agreements, and local government investment pools.

Specifically, Government money market funds (15.1(e)(1)) must:

- be registered as a mutual fund with the Securities and Exchange Commission (SEC) and operated in accordance with 17 CFR sec. 270.2a7 (2a7);
- be rated by a nationally recognized statistical rating organization: i.e., Standard & Poors, Moody's, Fitch;
- have their portfolio limited to U.S. government securities as defined in 2a7 and repurchase agreements collateralized by such U.S. securities.

Repurchase agreements (15.1(a)(8)) must comply with the following conditions:

- the underlying securities are permitted investments, pursuant to the list contained in Section B (Permitted Investments) above (15.1(a));
- the custody of the collateral is transferred to a third party. This means the bank must contract with a trusted third party to hold the collateral to ensure it is not pledged against any other investments;
- the maturity of the agreement is not more than 30 days;
- the underlying securities are purchased through a GUDPA bank; and
- a master repurchase agreement providing for the custody and security of collateral is executed.

Local Government Investment Pools (LGIP) (15.1(e)(2)) are subject to the following requirements:

- it is managed in accordance with the SEC's government money market rules (2a7);
- it is rated in the highest category by a nationally recognized statistical rating organization;

- it is limited to investments in U.S. Government securities that meet the definition of an eligible security, pursuant to 2a7, and repurchase agreements that are collateralized by such U.S. Government securities in which direct investment may be made pursuant to paragraphs (1) and (3) of 15.1(a);
- it is in compliance with the rules adopted by the Local Finance Board. These rules, expected to be adopted by early 1998, will provide for disclosure and reporting requirements, and other provisions to provide for the safety, liquidity, and yield of the investments. Until that time, the existing pools are permitted to continue to operate, though subject to the requirements of the statute;
- it does not permit investments in derivative instruments;
- pools have limits on the types of financial institutions from which they must purchase and redeem investments. The Division understands that existing pools currently comply with the criteria in the act.

LGIP's must comply with certain requirements for broker/dealers they utilize. At the time the investment is purchased or redeemed by a LGIP, the broker/dealer must have:

- been registered continuously for a period of at least two years, pursuant to section 9 of P.L. 1967, c. 93 (C. 49:3-56) and;
- have at least \$25 million in capital stock (or equivalent capitalization if not a corporation), surplus reserves for contingencies and undivided profits, or
- be a securities dealer who makes primary markets in U.S. Government securities and reports daily to the Federal Reserve Bank of New York its position in and borrowing on such U.S. Government securities.

### *E. Cash Management Plans and Policies*

N.J.S.A. 40A:5-14

Every local government unit must have a cash management plan. A cash management plan lists the GUDPA approved depository banks, any broker/dealers, and the approved investment instruments selected by the local unit's governing body. The cash management plan is adopted by resolution, usually at the reorganization meeting, or first meeting of the year. The cash management plan will guide the investment of the local unit's idle cash during periods that it is not needed to meet obligations.

The annual cash management plan may be amended at any time during the year to reflect changes due to changes in laws, depositories, funds, or investments. The inclusion of banks in the plan would eliminate separate bank resolutions passed each year. The Chief financial officer is charged with the administration of the plan.

When authorized, the cash management plan must include the designation of any government money market funds, and the designation of any other instruments permitted by (15.1(a)). This has particular relevance when investing in Federal and State agency or instrumentality obligations, or obligations that have unique requirements attached to them. These instruments are issued with a wide range of features or conditions, and have varying risk profiles. Therefore, the cash management plan, must provide precise guidance or specify the type, class, or features of those obligations for which investment is authorized.

The cash management plan is subject to audit. In addition, when the plan permits investments for more than one year, the investment must approximate the prospective use of the funds. This primarily relates to U.S. securities and local bond issue purchases. The law also requires that cash management plans provide for the CFO to give the governing body a monthly report that summarizes:

- all investments made or redeemed over the past month;
- each organization holding local unit funds;
- the amount of securities purchased or sold, class or type of securities purchased, book value, earned income, fees incurred, and market value of all investments as of the report date and;
- other information that may be required by the governing body.

An important factor for Chief Financial Officers to keep in mind is that N.J.S.A. 40A:5-14f provides that as long as local unit funds are deposited or invested as designated or authorized by the cash management plan, the CFO is relieved of any liability for any loss of such moneys due to the insolvency or closing of any depository designated by, or for the decrease in value of any investment authorized by, the cash management plan.

Local government units that actively manage their funds, should include a cash management policy as part of its plan. A cash management policy is the philosophy behind the cash management plan, and guides the construction and implementation of the cash management plan. To guide the CFO in making investments, cash management policies may include any of the following optional items:

- Authorization of specific investments, adding detail to the general provisions of the plan.
- Set policies for selecting and evaluating instruments, which shall consider the following factors:
  - Preservation of capital: this means the principal invested is safe and secure;
  - Liquidity: this means the ease with which the security can be converted to cash;
  - Current and historical investment returns: this means a comparison of current to past investment returns;
  - Diversification: this means spreading the investment principal among a number of investment instruments;
  - Maturity requirements: this means timing the maturity of the investment to match the need for the cash;
  - Costs and fees: this means the expenses associated with buying, storing, and redeeming investment instruments;

- Where appropriate, there should be professional investment administrators or advisors (see below).

### *F. Use of Investment Advisors*

If a municipality chooses to utilize the services of an investment advisor, local officials must know that investment advisors **must** be registered with the New Jersey Bureau of Securities (pursuant to N.J.S.A. 49:3-56), or with the Securities and Exchange Commission, unless exempt from registration. The law concerning regulation of investment advisors recently changed with enactment of the National Securities Markets Improvement Act amendments, which became effective on July 8, 1997. Similarly, broker-dealers can provide investment advice, provided they are registered with the Bureau.

N.J.S.A. 49:3-49(g) defines an investment advisor as follows:

"Investment advisor" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing or selling securities, or who, for compensation and as a part of a regular business, issues or promulgates analyses or reports concerning securities.

The Bureau of Securities (part of the State Department of Law and Public Safety, Division of Consumer Affairs), can provide the registration status as well as disciplinary information on any broker-dealers, agents of broker-dealers, and investment advisors. To check a broker-dealer, agent, or investment advisor, or to report suspected securities fraud, contact the Bureau at the address or telephone number that appears at the end of this Notice. Local units should feel free to contact the Bureau for assistance or questions about any such individuals to ensure they are registered to conduct business in the State.

Further, because of the State regulation, investment advisors are considered as professionals and contracts for their services are to be made pursuant to the professional services section of the Local Public Contracts Law (N.J.S.A. 40A:11-5(1)(a)(i)).

### *G. Investments and Risk*

This law was under consideration for over a year. A great deal of interest in it was expressed by all segments of the investment industry. Local elected officials and chief financial officers can expect to be solicited by a wide range of individuals and organizations offering their services. This includes direct sellers of mutual funds selling their government money market funds, local government investment pools, banks selling repurchase agreements, and broker-dealers selling permitted securities, in addition to services currently provided by GUDPA banks. As in the purchase of any goods or services, local officials should utilize prudence when a sales representative offers an investment program that promises above average returns, or something special that no one else can offer.

The investment of public funds has become a highly competitive industry. When considering where public funds will be invested, CFO's and governing body members should keep in mind the following investment issues :

- Recognize that *security* comes first, followed by *liquidity*, then *yield*.
- What is the fee structure? Is a government money market fund a load (fee up front) or no-load (fee is covered as part of the yield) fund; and what are the fees for getting into an investment, or getting out of it?
- "Past performance is not a guarantee of future results." While sometimes a cliché, it is important. Since government money market funds are required to be rated, study the ratings of funds: what has been their performance, what have their expenses been, what is the experience of their managers. These are questions that prudent investors ask before making investments.
- Use the New Jersey Cash Management Fund as a benchmark for comparing performance of money market or LGIP's. The fund has a wider variety of investments available to it than LGIP's or money market funds, and can be used as a reliable indicator of market performance.
- "If you can't explain it, you shouldn't buy it." A good rule of thumb regarding any investment instrument is that if you don't understand it yourself, and cannot explain it to someone else, you should not be buying it.

As noted above, local officials may be solicited by financial advisors to assist them in their investment decisions. In addition to the suggestions noted above, be prudent in taking their advice and consider what they are selling, how will they profit from it, what are their fees, and beware of churning (generation of excess fees by moving from investment to investment).

It is incumbent on the Chief Financial Officer and any elected officials involved in the process to understand the financial product being purchased if it is permitted under law, how the product is priced, the effect of interest rate changes on the value of the product, and the liquidity of the product. Care should also be taken with the purchase of any proprietary product, because the local unit will, in all probability, be only able to sell the product back to the broker-dealer that sold it in the first place. Advice of appropriate counsel should also be requested whenever there is a question about the legal status of an investment instrument.

The GFOA of the United States and Canada has excellent publications on hiring investment advisors that can be useful if you choose to utilize such services. Be sure to utilize the services of the Bureau of Securities when it comes to ensuring that investment advisors, or broker-dealers and agents of broker-dealers are registered, pursuant to law.

### *H. Other Concerns*

The law has a provision to prevent conflicts of interest in the investment of the local unit's funds. Any official involved in the designation of depositories or in the authorization of investments as permitted by 15.1(a), or in the selection of an entity seeking to sell securities to the local unit, who has a material business or personal relationship with that organization, shall disclose that relationship to the governing body of the local unit and to the Local Finance Board or a county or municipal ethics board, as appropriate. The officials covered by this ~~include the CFO and the governing body.~~ Until formal rules are adopted, this is to be done, in writing, to the Clerk of the local unit and to the Local Finance Board.

In addition, the registered principal officer of any securities brokerage firm (broker-dealer) selling securities to the local unit shall be provided with, and sign an acknowledgment that the principal has seen and reviewed, the local unit's cash management plan. If the firm is only selling a government money market fund, then the registered principal officer must be provided with, and sign an acknowledgment that, the government money market mutual fund being sold to the local unit meets the criteria of a government money market mutual fund, as permitted by (15.1(8)(1)). Notwithstanding these dictates, and while not required by the law, local units should consider providing any broker/dealer, with whom it conducts business, a copy of the cash management plan and policies, and have them certify that they have reviewed it and agree to follow its requirements. That will tend to ensure reliability of advice and provide legal backup in the event problems arise later.

Finally, local unit officials may be solicited by banks or brokers offering "highly competitive" repurchase agreement arrangements (repos) or other investments. Remember, something that seems too good to be true, probably isn't. This maxim comes into play in two particular areas.

The first is that the law requires that all repos be purchased through GUDPA approved banks, which means they must do business in the State and participate in the GUDPA Program. That eliminates the purchase of repos from out of state banks. In addition, all repos must be collateralized with the collateral held by a third party. All local units investment in repos **must** have master agreements (usually a standard form) that provides the agreement for custody and security of the collateral.

While broker-dealers are qualified as professional services, they are NOT permitted depositories of funds, and certificates of deposits or repurchase agreements CANNOT be purchased from them. This prohibition also applies to broker-dealers attached to banks; CD's and repo's can only be purchased from the bank, not any broker-dealer organization that is co-located with them or a subsidiary organization of the bank.

The second is when a broker-dealer assures the local government unit that an investment "is just like" or is the "same as" a permitted investment, but will produce a higher return. If the broker-dealer is making that type of promise or assurance, it is probably NOT the same, is more than likely NOT permitted under the law, and probably has a higher risk profile than the type of investment that is permitted, which is how it will out-perform the permitted investment. The investment of public funds is too important an endeavor to put careers or public funds at risk, particularly for a small increase in investment return. When you have questions about permissibility of investments or broker-dealers, contact this Division, the Division of Investments, the Bureau of Securities and utilize competent legal counsel.

The Division of Investments can provide information about the permissibility of federal instruments and grant approval for other investments that are permitted under the law. As described above, the Bureau of

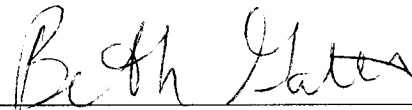


Securities can provide information on the registration status as well as disciplinary information, if any, on broker-dealers and their agents, and investment advisors. Their contacts and addresses follow:

Roland M. Machold, Director  
Division of Investments  
P.O. Box 290  
Trenton, New Jersey 08625  
(609) 292-5106

Franklin L. Widmann, Chief  
Bureau of Securities  
P.O. Box 47029  
Newark, New Jersey 07101  
(973) 504-3600

We hope that the foregoing information proves to be helpful. If you have any questions, contact the Division at (609) 292-0506.



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Beth Gates, Director  
Division of Local Government Services

Enclosure

Distribution: Chief Financial Officers of Municipalities, Counties, Authorities, and Fire Districts

## *Appendix A*

### **U.S. FEDERAL AGENCY DEBT: SELECTED MARKET TERMINOLOGY EXPLAINED**

The following explanation is not based on legal analysis, rather, it focuses on terms used in the capital markets since little information about the meaning and use of these terms is readily available. New Jersey law permits investment in:

"Any federal agency or instrumentality obligation authorized by Congress that matures within 397 days from the date of purchase, and has a fixed rate of interest not dependent on any index or external factors."

The following terms should assist local officials in determining what federal obligations meet this criteria.

#### ***AGENCY***

An agency of the U.S. government performs a function for the government. For example, departments of the Executive Branch, such as State, Treasury, Labor, and Housing and Urban Development, are examples of agencies of the federal government. A list of federal agencies can be found in the U.S. Code of Federal Regulations.

The term agency, when used with federally related entities, is not entirely accurate, but is derived from references in authorizing legislation. Characteristics of debt and mortgage-backed securities issues from Government Sponsored Entities (see below) can be similar to those of federal government securities (see Agency Status).

#### ***AGENCY STATUS***

Agency status applies to characteristics listed in legislation or regulation that allow certain securities of federal government related entities to enter the market with attributes of U.S. government securities. Major elements are:

- Exempt from SEC registration;
- Legal for investment by U.S. financial institutions, such as national banks, savings and loans, and credit unions;
- Issued and payable through the Federal Reserve;
- Eligible to be purchased and held by U.S. national banks without limitations;
- Exempt from U.S. state and local taxes;
- Eligible collateral for U.S. Treasury tax and loan accounts in the U.S.;
- Eligible for open market purchases in the U.S.;
- Eligible for U.S. national bank repurchase agreements (repos) without reserve requirements; and
- Eligible for private repos in (outside of the margin rules) the U.S.

## ***INSTRUMENTALITY***

An instrumentality is an entity through which the federal government carries out some of its functions. For example, the Federal Home Loan Banks are described as U.S. instrumentalities. Federal entities that serve a government purpose and are not agencies are generally referred to as instrumentalities. This includes government sponsored enterprises (below).

## ***GOVERNMENT-SPONSORED ENTERPRISE***

The term government-sponsored enterprise (GSE) has been used to describe certain off-budget entities created by the U.S. Congress. While existing GSE securities do not have the explicit full faith and credit support of the U.S. government, however, *they are permitted investments as federal instrumentalities*. The group of entities normally identified as GSEs are:

- Federal Farm Credit Banks,
- Federal Home Loan Banks,
- Federal Home Loan Mortgage Corp. (FHLMC, or Freddie Mac),
- Federal National Mortgage Association (FNMA, or Fannie Mae), and
- Student Loan Marketing Association (SLMA, or Sallie Mae).

In 1996, (Congress passed legislation that provided for the privatization of SLMA. However, that legislation maintains the legal status of SLMA's GSE debt.

**Excerpted from** Standard and Poors Managed Funds, Criteria and Related Analytics. August 1997..

**P.L. 1997, Chapter 148**  
**enacted June 30, 1997**

AN ACT concerning the investment powers of boards of education and local units and amending P.L. 1977, c.177 and P.L.1977, c.396.

BE IT ENACTED by the Senate and General Assembly of the State of New Jersey:

**1. 18A:20-37 (Section 1 of P.L. 1977, c.177) is amended to read as follows:**

a. When authorized by a resolution adopted by a majority vote of all its members the board of education of any school district may use moneys which may be in hand for the purchase of the following types of securities which, if suitable for registry, may be registered in the name of the school district:

(1) Bonds or other obligations of the United States of America or obligations guaranteed by the United States of America;

(2) Government money market mutual funds;

(3) Any obligation that a federal agency or a federal

instrumentality has issued in accordance with an act of Congress, which security has a maturity date not greater than 397 days from the date of purchase, provided that such obligation bears a fixed rate of interest not dependent on any index or other external factor;

(4) Bonds or other obligations of the local unit or bonds or other obligations of school districts of which the local unit is a part or within which the school district is located;

(5) Bonds or other obligations, having a maturity date not more than 397 days from the date of purchase, approved by the Division of Investment of the Department of the Treasury for investment by local units;

(6) Local government investment pools;

(7) Deposits with the State of New Jersey Cash Management Fund established pursuant to section 1 of P.L. 1977, c.281 (C.52:18A-90.4); or

(8) Agreements for the repurchase of fully collateralized securities, if:

(a) the underlying securities are permitted investments

pursuant to paragraphs (1) and (3) of this subsection a.;

(b) the custody of collateral is transferred to a third party;

(c) the maturity of the agreement is not more than 30 days;

(d) the underlying securities are purchased through a public depository as defined in section 1 of P.L. 1970, c.236 (C.17:9-41); and

(c) a master repurchase agreement providing for the custody and security of collateral is executed.

b. Any investment instruments in which the security is not physically held by the school district shall be covered by a third party custodial agreement which shall provide for the designation of such investments in the name of the school board and prevent unauthorized use of such investments.

c. Purchase of investment securities shall be executed by the "delivery versus payment" method to ensure that securities are either received by the school district or a third party custodian prior to or upon the release of the school district's funds.

d. Any investments not purchased and redeemed directly from the issuer, government money market mutual fund, local government investment pool, or the State of New Jersey Cash Management Fund, shall be purchased and redeemed through the use of a national or State bank located within this State or through a broker-dealer which, at the time of purchase or redemption, has been registered continuously for a period of at least two years pursuant to section 9 of P.L. 1967, c.93 (C.49:3-5) and has at least \$25 million in capital stock (or equivalent capitalization if not a corporation), surplus reserves for contingencies and undivided profits, or through a securities dealer who makes primary markets in U.S. Government securities and reports daily to the Federal Reserve Bank of New York its position in and borrowing on such U.S. Government securities.

e. For the purposes of this section:

(1) a "government money market mutual fund" means an investment company or investment trust:

(a) which is registered with the Securities and Exchange Commission under the "Investment Company Act of 1940," 15 U.S.C. sec. 80a-1 et seq., and operated in accordance with 17 C.F.R. sec. 270.2a-7;

(b) the portfolio of which is limited to U.S. Government securities that meet the definition of an eligible security pursuant to 17 C.F.R. sec. 270.2a-7 and repurchase agreements that are collateralized by such U.S. Government securities in which direct investment may be made pursuant to paragraphs (1) and (3) of subsection (a) of this section; and

(c) which is rated by a nationally recognize statistical rating organization.

(2) a "local government investment pool" means an investment pool:

(a) which is managed in accordance with 17 C.F.R. 270.2a-7;

(b) which is rated in the highest category by a nationally recognized statistical rating organization;

(c) which is limited to U.S. Government securities that meet the definition of an eligible security pursuant to 17 C.F.R. sec. 270.2a-7 and repurchase agreements that are collateralized by such U.S. Government securities in which direct investment may be made pursuant to paragraphs (1) and (3) of subsection (a) of this section;

(d) which is in compliance with rules adopted pursuant to the "Administrative Procedure Act," P.L. 1968, c.410 (C.52:14B-1 et seq.) by the Local Finance Board of the Division of Local Government Services in the Department of Community Affairs, which rules shall provide for disclosure and reporting requirements, and other provisions deemed necessary by the board to provide for the safety, liquidity and yield of the investments;

(e) which does not permit investments in instruments that: are subject to high price volatility with changing market conditions; cannot reasonably be expected, at the time of interest rate adjustment, to have a market value that approximates their par value; or utilize an index that does not support a stable net asset value; and

(f) which purchases and redeems investments directly from the issuer, government money market mutual fund, or the State of New Jersey Cash Management Fund, or through the use of a national or State bank located within this State, or through a broker-dealer which, at the time of purchase or redemption, has been registered continuously for a period of at least two years pursuant to section 9 of P.L. 1967, c.93 (C.49:3-56) and has at least \$25 million in capital stock (or equivalent capitalization if not a corporation), surplus reserves for contingencies and undivided profits, or through a securities dealer who makes primary markets in U.S. Government securities and reports daily to the Federal Reserve Bank of New York its position in and borrowing on such U.S. Government securities.

f. Investments in, or deposits or purchases of financial instruments made pursuant to this section shall not be subject to the requirements of the "Public School Contracts Law," N.J.S. 18A:18A-1 et seq.

**Section 2. N.J.S.40A:5-14 is amended to read as follows:**

40A:5-14. Cash management plan

a. Each local unit shall adopt a cash management plan and shall deposit, or invest, or both deposit and invest, its funds pursuant to that plan. The cash management plan shall include:

(1) the designation of a public depository or depositories as defined in section 1 of P.L. 1970, c.236 (C.17:9-41) and may permit deposits in such public depository or depositories as permitted in section 4 of P.L. 1970, c.236 (C.17:9-44);

(2) the designation of any fund that meets the requirements established pursuant to section 8 of P.L. 1977, c.396 (C.40A:5-15.1) and the authorization for investments as permitted pursuant to section 8 of P.L. 1977, c.396 (C.40A:5-15.1); or

(3) any combination of the designations or authorizations permitted pursuant to this subsection a.

b. The cash management plan shall be approved annually by majority vote of the governing body of the local unit and may be modified from time to time in order to reflect changes in federal or State law or regulations, or in the designations of depositories, funds or investment instruments or the authorization for investments. The chief financial officer of the local unit shall be charged with administering the plan.

c. The cash management plan shall be designed to assure to the extent practicable the investment of local funds in interest bearing accounts and other permitted investments. The cash management plan shall be subject to the annual audit conducted pursuant to N.J.S.40A:5-4. When an investment in bonds maturing in more than one year is authorized, the maturity of those bonds shall approximate the prospective use of the funds invested.

d. The cash management plan may include authorization to invest in any of the investments authorized pursuant to section 8 of P.L. 1977, c.396 (C.40A:5-15.1) and shall set policies for selecting and evaluating investment instruments accordingly. Such policies shall consider preservation of capital, liquidity, current and historical investment returns, diversification, maturity requirements, costs and fees, and when appropriate, policies of investment instrument administrators. Policies shall be based on a cash flow analysis prepared by the chief financial officer and be commensurate with the nature and size of the funds held by the local unit. All investments shall be made on a competitive basis insofar as practicable.

e. The cash management plan shall require a monthly report to the governing body summarizing all investments made or redeemed since the last meeting. The report shall set forth each organization holding local unit funds, the amount of securities purchased or sold, class or type of securities purchased,

book value, earned income, fees incurred, and market value of all investments as of the report date and other information that may be required by the governing body.

f. The official charged with the custody of moneys of a local unit shall deposit or invest them as designated or authorized by the cash management plan pursuant to subsection a. of this section and shall thereafter be relieved of any liability for loss of such moneys due to the insolvency or closing of any depository designated by, or the decrease in value of any investment authorized by, the cash management plan pursuant to subsection a. of this section.

g. Any official involved in the designation of depositories or in the authorization for investments as permitted pursuant to section 8 of P.L. 1977, c.396 (C.40A:5-15.1), or any combination of the preceding, or the selection of an entity seeking to sell an investment to the local unit who has a material business or personal relationship with that organization shall disclose that relationship to the governing body of the local unit and to the Local Finance Board or a county or municipal ethics board, as appropriate.

h. The registered principal of any security brokerage firm selling securities to the local unit shall be provided with, and sign an acknowledgment that the principal has seen and reviewed the local unit's cash management plan, except that with respect to the sale of a government money market mutual fund, the registered principal need only be provided with and sign an acknowledgment that the government money market mutual fund whose securities are being sold to the local unit meets the criteria of a government money market mutual fund as set forth in paragraph (1) of subsection e. of section 8 of P.L. 1977, c.396 (C.40A:5-15.1).

(cf. P.L. 1983, c.8, s.2)

**3. 40A:5-15.1 is amended to read as follows:**

40A:5-15.1 Securities which may be purchased by local units.

a. When authorized by a cash management plan approved pursuant to N.J.S. 40A:5-14, any local unit may use moneys which may be in hand for the purchase of the following types of securities which, if suitable for registry, may be registered in the name of the local unit:

(1) Bonds or other obligations of the United States of America or obligations guaranteed by the United States of America;

(2) Government money market mutual funds;

(3) Any obligation that a federal agency or a federal instrumentality has issued in accordance with an act of Congress, which security has a maturity date not greater than 397 days from the date of purchase, provided that such obligation bears a fixed rate of interest not dependent on any index or other external factor;

(4) Bonds or other obligations of the local unit or bonds or other obligations of school districts of which the local unit is a part or within which the school district is located;

(5) Bonds or other obligations, having a maturity date not more than 397 days from the date of purchase, approved by the Division of Investment of the Department of the Treasury for investment by local units;

(6) Local government investment pools;

(7) Deposits with the State of New Jersey Cash Management Fund established pursuant to section 1 of P.L. 1977, c.281 (C.52:18A-90.4); or

(8) Agreements for the repurchase of fully collateralized

securities, if:

(a) the underlying securities are permitted investments pursuant to paragraphs (1) and (3) of this subsection a.;

(b) the custody of collateral is transferred to a third party;

(c) the maturity of the agreement is not more than 30 days;

(d) the underlying securities are purchased through a public depository as defined in section 1 of P.L. 1970, c.236 (C.17:9-41); and

(e) a master repurchase agreement providing for the custody and security of collateral is executed.

b. Any investment instruments in which the security is not physically held by the local unit shall be covered by a third party custodial agreement which shall provide for the designation of such investments in the name of the local unit and prevent unauthorized use of such investments.

c. Purchase of investment securities shall be executed by the "delivery versus payment" method to ensure that securities are either received by the local unit or a third party custodian prior to or upon the release of the local unit's funds.

d. Any investments not purchased and redeemed directly from the issuer, government money market mutual fund, local government investment pool, or the State of New Jersey Cash Management Fund, shall be purchased and redeemed through the use of a national or State bank located within this State or through a broker-dealer which, at the time of purchase or redemption, has been

registered continuously for a period of at least two years pursuant to section 9 of P.L. 1967, c. 93 (C.49:3-5) and has at least \$25 million in capital stock (or equivalent capitalization if not a corporation), surplus reserves for contingencies and undivided profits, or through a securities dealer who makes primary markets in U.S. Government securities and reports daily to the Federal Reserve Bank of New York its position in and borrowing on such U.S. Government securities.

e. For the purposes of this section:

(1) a "government money market mutual fund" means an investment company or investment trust:

(a) which is registered with the Securities and Exchange Commission under the "Investment Company Act of 1940," 15 U.S.C. sec. 80a-1 et seq., and operated in accordance with 17 C.F.R. sec. 270.2a-7;

(b) the portfolio of which is limited to U.S. Government securities that meet the definition of an eligible security pursuant to 17 C.F.R. sec. 270.2a-7 and repurchase agreements that are collateralized by such U.S. Government securities in which direct investment may be made pursuant to paragraphs (1) and (3) of subsection (a) of this section; and

(c) which is rated by a nationally recognize statistical rating organization.

(2) a "local government investment pool" means an investment pool:

(a) which is managed in accordance with 17 C.F.R. 270.2a-7;

(b) which is rated in the highest category by a nationally recognized statistical rating organization;

(c) which is limited to U.S. Government securities that meet the definition of an eligible security pursuant to 17 C.F.R. sec. 270.2a-7 and repurchase agreements that are collateralized by such U.S. Government securities in which direct investment may be made pursuant to paragraphs (1) and (3) of subsection (a) of this section;

(d) which is in compliance with rules adopted pursuant to the "Administrative Procedure Act," P.L. 1968, c. 410 (C.52:14B-1 et seq.) by the Local Finance Board of the Division of Local Government Services in the Department of Community Affairs, which rules shall provide for disclosure and reporting requirements, and other provisions deemed necessary by the board to provide for the safety, liquidity and yield of the investments;

(e) which does not permit investments in instruments that are subject to high price volatility with changing market conditions; cannot reasonably be expected, at the time of interest rate adjustment, to have a market value that approximates their par value; or utilize an index that does not support a stable net asset value; and

(f) which purchases and redeems investments directly from the issuer, government money market mutual fund, or the ate of New Jersey Cash Management Fund, or through the use of a national or State bank located within this State, or through a broker-dealer which, at the time of purchase or redemption, has been registered continuously for a period of at least two years pursuant to section 9 of P.L. 1967, c. 93 (C.49:3-56) and has at least \$25 million in capital stock (or equivalent capitalization if not a corporation), surplus reserves for contingencies and undivided profits, or through a securities dealer who makes primary markets in U.S. Government securities and reports daily to the Federal Reserve Bank of New York its position in and borrowing on such U.S. Government securities.

f. Investments in, or deposits or purchases of financial instruments made pursuant to this section shall not be subject to the requirements of the "Local Public Contracts Law," P.L. 1971, c. 198 (C.40A:11-1 et seq.). (cf. P.L. 1991, c. 458, s.2)