

## NOTE 2. CASH, INVESTMENTS AND RESTRICTED ASSETS

**The Cash Management Policy Board:** The policy for the investment of State funds is the responsibility of the Cash Management Policy Board (the Board). The Board, created by State law, establishes policies for and the terms, conditions, and other matters relating to, the investment of all money belonging to the State except money in the DPERS and money held under the State deferred compensation program.

**Investment Guidelines and Management:** The investment guidelines, adopted by the Board provide, among other things, that no more than 10% of the portfolio may be invested in obligations of any one issuer other than the U.S. Government. Investments may be made only in fixed income instruments with maturities of up to five years in certain circumstances.

**Collateralization Requirements:** All State funds are required by law to be collateralized by direct obligations of, or obligations which are guaranteed by, the United States of America, or other suitable obligations as determined by the Board, unless the Board shall find such collateralization not in the best interest of the State. The Board has determined that certificates of deposit and time deposits must be collateralized unless the bank issuing the certificate has assets of not less than \$5 billion and is rated not lower than "B" by Keefe, Bruyette & Wood's Bank Watch Service. The Board has also determined that State demand deposits need not be collateralized provided that any bank that holds these funds has for the last two years, a return on average assets of 5% or greater and an average equity-capital ratio of at least 1:20. If the bank does not meet the above criteria, collateral must consist of one or more of the following:

- (a) U.S. Government securities;
- (b) U.S. Government agency securities;
- (c) State of Delaware securities; or
- (d) Securities of a political subdivision of the State with a Moody's Investors Service rating of "A" or better.

Additionally, the bank must ensure that those securities pledged as collateral have a market value equal to or greater than 102% of the ledger balance(s) in the account(s) each day and ensure that securities pledged are identified as held in the State's name and are segregated on the bank's records.

Cash and Cash Equivalents consist of demand deposits, short-term money market funds and other deposits held by financial institutions, generally with a maturity of

three months or less when purchased. Cash and cash equivalents are reported as deposits.

Cash and Cash Equivalents as reported on the statement of net assets, may be under the control of the State Treasurer or other administrative bodies as determined by the Cash Management Policy Board. All cash deposited with the State Treasurer by State agencies is maintained by the Treasurer in various pooled investment funds (State Investment Pool). The State Treasurer invests the deposited cash including the cash float in short-term securities and other investments.

An analysis of cash and investments by category of risk as required by GASB Statement No. 3 is presented below .

## **(A) DEPOSITS**

### **Primary Government**

At June 30, 2003, the carrying value and the bank balances of the State's deposits were \$814,901,000 and \$820,926,000 respectively. Of the bank balances, \$17,843,000 was insured by the Federal Deposit Insurance Corporation (FDIC) and/or collateralized with securities held by the State or by its agent in the State's name (Category 1). \$537,060,000 is uninsured and uncollateralized (Category 3). The remaining \$266,023,000 represents unemployment insurance taxes collected from Delaware employers that are held in escrow by the U.S. Treasury.

As a condition for operating in the State, various insurance companies have deposited an aggregate amount of \$395,525,000 into escrow. The State Insurance Commission and the insurance companies are joint custodians of such funds. Because the State can neither use nor release these funds without the joint approval of the insurer/depositor, these amounts are not reported in the State's financial statements.

### **Component Units**

#### **Delaware State Housing Authority**

The Delaware State Housing Authority's deposits for risk categorization consist of checking accounts, money market accounts, bank savings accounts and investment agreements. The total carrying value and bank balance of the deposits at June 30, 2003 was \$53,200,114, and \$53,800,289 respectively. Of the bank balance, \$1,499,555 was entirely insured or collateralized with securities held by the Authority or by its agent in the Authority's name (Category 1). The remaining \$52,300,734 consists of investment agreements that are neither insured nor collateralized (Category 3). For purposes of the financial statements, money market accounts,

bank savings are classified as investments and investment agreements are classified as restricted investments.

#### Diamond State Port Corporation

At June 30, 2003, the carrying value and bank balances of the Diamond State Port Corporation's cash deposits amounted to \$1,404,581 and \$1,600,427, respectively. Of the bank balances, \$100,000 is insured by the FDIC (Category 1) and the remaining \$1,500,427 is uninsured and uncollateralized (Category 3). \$222,330 of restricted cash and cash equivalents consists of short-term investments.

#### Riverfront Development Corporation

At June 30, 2003, the Riverfront Development Corporation's cash deposits carrying value and bank balances amounted to \$190,513 and \$333,457 respectively. Cash deposits include \$96,689 of restricted cash and cash equivalents. Of the bank balances, \$201,685 is insured by the FDIC (Category 1) and \$127,200 is uninsured and uncollateralized (Category 3). The remaining \$4,572 consists of deposits included in the State Investment Pool.

#### Delaware State University

At June 30, 2003, Delaware State University's deposits carrying value and bank balance was \$5,417,178 and \$3,396,556 respectively. An additional \$6,138,190 of cash and cash equivalents related to unexpended State appropriations are included on the Statement of Net Assets. Of the bank balances, \$100,000 was insured by FDIC (Category 1) and the remaining \$3,296,556 was uninsured and uncollateralized (Category 3).

#### Delaware Charter Schools

At June 30, 2003, the Delaware Charter Schools deposits carrying value was \$8,242,000, consisting entirely of deposits included in the State Investment Pool.

## **B. INVESTMENTS**

### **Primary Government**

The table on the following page provides information about the custodial credit risks associated with the State's investments. Category 1 includes investments that are insured or registered or for which the securities are held by the State or its agent in the State's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent

in the State's name. As of June 30, 2003 the State does not have any investments in Category 2. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the State's name.

The State's Investments below include \$12,325,000 presented as restricted assets on the balance sheet. Pooled investments represent those investments in units of a pool rather than specific securities. As a result, such investments are not categorized as to risk because they are not evidenced by securities that exist in a physical or book-entry form.

### PRIMARY GOVERNMENT INVESTMENTS

( Expressed in Thousands)

Investment Type	Category		Total Fair Value
	1	3	
Commercial Paper	\$ 226,818	\$ 28,009	\$ 254,827
U.S. Government Agency Securities	162,186	479,372	641,558
Corporate Obligations		239,231	239,231
Foreign Government Securities		15,680	15,680
Municipal Bonds		13,994	13,994
Pension and Investment Trust Funds:			
Domestic Fixed Income	931,235		931,235
Domestic Equities	1,195,211		1,195,211
Short Term Investments *	123,190		123,190
Managed Futures	103,462		103,462
Foreign Equities	362,493		362,493
SUBTOTAL	<u>\$ 2,755,577</u>	<u>\$ 729,242</u>	3,880,881
Pooled Investments not subject to categorization: **			
Pooled Investments			14,770
Pension and Investment Trust Investment Pool:			
Pooled Equity & Fixed Income			1,708,682
Private Investments			456,366
SUBTOTAL INVESTMENTS			\$ 6,060,699
Less: Pooled Component Unit Investments			(55,140)
TOTAL STATE INVESTMENTS ***			<u>\$ 6,005,559</u>

\* Pension Short Term Investments primarily include Commercial Paper and overnight deposits.

\*\* Investments not evidenced by securities are not categorized.

\*\*\* Includes investments classified as restricted assets on the Statement of Net Assets.

	<b>Governmental Activities</b>	<b>Business Type Activities</b>	<b>Fiduciary Funds</b>	<b>Totals</b>
Cash/Cash Equivalents	\$ 505,117	\$ 282,345	\$ 26,366	\$ 813,828
Restricted Cash/Cash Equivalents		1,073		1,073
Short Term Investments	100,753	292,938	8,847	402,538
Long Term Investments	644,298	65,759		710,057
Restricted Investments		12,325	4,880,639	4,892,964
	<u>\$ 1,250,168</u>	<u>\$ 654,440</u>	<u>\$ 4,915,852</u>	<u>\$ 6,820,460</u>
	Less: Carry Value of Deposits			(814,901)
	Balance In State Investment Pool			<u>\$ 6,005,559</u>

The pooled investments of the pension and investment trust funds consist primarily of venture capital, limited partnerships, open-end mutual funds and real estate. The fair value of pension and investment trust investments is determined by quoted market values, where applicable. Investments in real estate pooled funds are determined based on appraised values. Venture capital and other limited partnership values are determined based on discounted market values where market quotes are available, and by various procedures for investments in non-traded partnerships where quotes are not available. In 1994, the Board of Pension Trustees of the DPERS adopted a formal written policy on the use of derivatives. Only a few selected managers are permitted to use derivatives. In every case, the types of derivatives used and limits on their use are spelled out in manager contracts and are monitored on an ongoing basis. The Board believes that it is unlikely that any of the derivatives used by managers of the DPERS could have a material adverse effect on the financial condition of the DPERS. Managers authorized to use derivatives do so to reduce foreign exchange risk and minimize transaction costs. Managers may also use derivatives as part of an overall strategy to enhance returns. The following lists principal categories of derivatives and their uses during the year:

<b>Category</b>	<b>Purpose</b>
Foreign exchange forward contracts	Hedge currency risk of investments denominated in foreign currencies
Exchange traded equity futures	Reduce transaction costs; hedge equity market risk; enhance return
Exchange traded fixed income futures	Reduce transaction costs; control portfolio duration; enhance return
Exchange traded options	Enhance return; reduce transaction costs
Asset backed securities	Enhance return

### ***Repurchase Agreements***

For repurchase agreements, the underlying securities consist of U.S. Government or government agency securities, certificates of deposit, commercial paper or bankers' acceptances. All repurchase transactions are governed by written repurchase agreements. Statutes require that securities underlying repurchase agreements must

have a market value of at least 102% of the cost of the repurchase agreement. Due to significantly higher cash flows at certain times during the fiscal year, the State's investment in overnight repurchase agreements for which the underlying securities were held by the dealer (Category 3) fluctuates.

### ***Reverse Repurchase Agreements***

The Cash Management Policy Board permits the State to enter into reverse repurchase agreements, that is, a sale of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest. At June 30, 2003, the State had no reverse repurchase agreements.

### **COMPONENT UNITS**

#### Delaware State Housing Authority

The Delaware State Housing Authority invests its funds and those held by its trustees in accordance with the various applicable bond resolutions, Federal laws and regulations, and is under the oversight of the State's Cash Management Policy Board. DSHA investments categorized as to risk had a fair value of \$91,757,092 at June 30, 2003. Of this amount, \$42,445,356 was uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the Authority's name (Category 3). The remaining \$49,311,736 represents pooled investments where the Authority does not own specific securities. This amount includes funds of \$40,755,769 specifically identified for the Authority in the State of Delaware's Investment Pool. These pooled investments are categorized by risk within the investments of the primary government.

#### Diamond State Port Corporation

The carrying and fair value of investments of the DSPC at June 30, 2003 amounted to \$2,888,965. The investments, consisting of various equity and mutual funds, are classified for credit risk as uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the DSPC's name (Category 3).

#### Delaware State University

Investments of the University totaled \$13,076,590, stated at quoted market value. These investments consist of pooled investments where the University does not own specific securities.