City of La Porte, Texas Investment Policy

Adopted by the City Council

Of the City of La Porte

On January 13, 1992, by

Ordinance No. 1802

Amended – November 1995

Amended – August 1997

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Amended - February 2003

City of La Porte, Texas

Cynthia B. Alexander Director of Finance

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I. POLICY

It is the policy of the City of La Porte, Texas (the "City") to administer and invest its funds in a manner which will preserve the principal and maintain the liquidity though limitations and diversification while meeting the daily cash flow requirements of the City. The City will conform to all statutes governing the investment of the City's funds, including, but not by way of limitation, the Public Funds Investment Act, Chapter 2256, Texas Government Code (the "Act").

II. SCOPE

The City will strive to earn a return on funds invested at the highest investment return possible after taking in consideration the primary goals of preservation of principal and liquidity of funds invested, consistent with the policy objectives described below. This investment policy applies to the investment activities of the government of the City of La Porte, Texas.

<u>FUNDS INCLUDED</u> All financial assets of all funds managed by the City, including but not limited to receipts of Tax Revenues, Charges for Services, Bond Proceeds, Interest Incomes, Loans and Funds received by the City where the City performs a custodial function.

III. OBJECTIVES

<u>SAFETY</u> The primary objective of the City's investment activity is the preservation of capital in the overall portfolio. Each investment transaction shall seek first to ensure that capital losses are avoided, whether they are from securities defaults or erosion of market value.

<u>LIQUIDITY</u> The City's investment portfolio will remain sufficiently liquid to enable the City to meet operating requirements that might be reasonably anticipated. Liquidity shall be achieved by matching investment maturities with forecasted cash flow requirements and by investing in securities with active secondary markets.

<u>YIELD</u> The City's cash management portfolio shall be designed with the objective of regularly exceeding the average rate of return on the three month U.S. Treasury Bill. The investment program shall seek to augment returns above this threshold consistent with risk limitations identified herein and prudent investment principles.

<u>RISK OF LOSS</u> All participants in the investment process shall seek to act responsibly as custodians of the public trust. Investment Officials shall avoid any transaction that might impair public confidence in the City's ability to govern effectively. The governing body recognizes that in a diversified portfolio, occasional measured losses due to market volatility are inevitable, and must be considered within the context of the overall portfolio's investment return, provided that adequate diversification has been implemented.

IV. OVERSIGHT RESPONSIBILITY

Oversight Responsibility for the investment activity of the City of La Porte shall rest with the Audit Committee and the City Manager.

V. RESPONSIBILITY AND CONTROL

<u>DELEGATION</u> Management responsibility for the investment program is hereby delegated to the Director of Finance, who shall establish written procedures for the operation of the investment program, consistent with this investment policy. Such procedures shall include explicit delegation of authority to persons responsible for investment transactions.

<u>SUBORDINATES</u> All persons involved in investment activities will be referred to as "Investment Officials." No person shall engage in an investment transaction except as provided under the terms of this policy and the procedures established by the Director of Finance. The Director of Finance shall be responsible for all transactions undertaken, and shall establish a system of controls to regulate the activities of Subordinate Investment Officials.

QUARTERLY REPORTS The Director of Finance shall submit quarterly an investment report that summarizes recent market conditions, economic developments and anticipated investment conditions. The report shall summarize the investment strategies employed in the most recent quarter, describe the portfolio in terms of investment securities, maturities, risk characteristics, book values, market values and other features. The report shall explain the quarter's total investment return and compare the return to budgetary expectations. The report shall include an appendix that discloses all transactions during the quarter.

<u>ANNUAL REPORTS</u> Within 90 days of the end of the fiscal year, the Director of Finance shall present a comprehensive annual report on the investment program and investment activity. The annual report shall include twelve-month and quarterly comparison of returns, and shall suggest improvements that might be made in the investment program.

<u>PRUDENCE</u> Investments shall be made with the exercise of due care, 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 own capital as well as the probable income to be derived. Investment Officials acting in accordance with written procedures and this investment policy and exercising due diligence shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and the liquidity and the sale of securities are carried out in accordance with the terms of this policy.

<u>CONFLICTS OF INTEREST</u> Officials and employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions.

<u>DISCLOSURE</u> Employees and Investment Officials shall disclose to the City Manager any material financial interests in financial institutions that conduct business with the City of La Porte, and shall further disclose any large financial or investment positions that could be related to the performance of the City's portfolio. Employees and Investment Officials shall subordinate their personal investment transactions to those of this jurisdiction, particularly with regard to the timing of purchases and sales.

<u>TRAINING</u> Investment Officials shall attend at least one investment training session within 12 months after taking office or assuming duties, and shall attend an investment training session not less than once in a two-year period and receive not less than 10 hours of instruction relating to investment responsibilities from an independent source approved by the audit committee. For the purposes of this policy, an "independent source" is defined as a professional organization, an

institute of higher learning or any other sponsor other than a Business Organization with whom the City may engage in investment transactions. Independent sources that may provide investment training include the Government Treasurer's Organization of Texas, the University of North Texas, the Government Finance Officers Association of Texas, or the Texas Municipal League. Training shall be in accordance with the Public Funds Investment Act and shall include education in investment controls, security risks, market risks, and compliance with statutes governing the investment of public funds.

VI. INVESTMENTS

<u>ACTIVE PORTFOLIO MANAGEMENT</u> The City intends to pursue active versus passive portfolio management philosophy. That is, securities may be sold before they mature if market conditions present an opportunity for the City to benefit from the trade.

<u>ELIGIBLE INVESTMENTS</u> Assets of funds of the government of the City of La Porte may be invested in the following as authorized by the Public Funds Investment Act:

A. Obligations of, or Guaranteed by Governmental Entities

- 1. Except as provided by Subsection 2, the following are authorized investments under this section:
 - a) obligations of the United States or its agencies and instrumentalities;
 - b) direct obligations of this state or its agencies and instrumentalities;
 - c) collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States;
 - d) other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, this state or the United States or their respective agencies and instrumentalities; and
 - e) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent.
- 2. The following are not authorized investments under this section:
 - a) obligations whose payment represents the coupon payment on the outstanding principal balance of the underlying mortgage-backed security collateral and pays not principal (Interest only bonded);
 - b) obligations whose payment represents the principal stream of cash from the underlying mortgage-backed security collateral and pays no interest (Principal only bonds):
 - c) collateralized mortgage obligations that have a final stated maturity date of greater that 10 years; and

d) collateralized mortgage obligations, the interest rate of which is determined by an index that adjusts opposite to the changes in a market index.

B. Certificate of Deposit and Share Certificates

- 1. A certificate of deposit is an authorized investment under this Subsection if the certificate is issued by a state or national bank domiciled in this state, a savings bank domiciled in this state, or a state or federal credit union domiciled in this state and is:
 - a) guaranteed or insured by the Federal Deposit Insurance Corporation or its successor or the National Credit Union Share Insurance Fund or its successor;
 - b) secured by obligations that are described by Subsection A, 1, including mortgage backed securities directly issued by a federal agency or instrumentality that have a market value of not less than the principal amount of the certificates, but excluding those mortgage backed securities of the nature described by Subsection A, 2; or
 - c) secured in any other manner and amount provided by law for deposits of the investing entity.

C. Repurchase Agreements

- 1. A fully collateralized repurchase agreement is an authorized investment under this Subsection if the repurchase agreement:
 - a) has a defined termination date;
 - b) is secured by obligations described by Subsection A, 1, a); and
 - c) requires the securities being purchased by the entity to be pledged to the entity, held in the entity's name, and deposited at the time the investment is made with the entity or with a third party selected and approved by the entity; and
 - d) is placed through a primary government securities dealer, as defined by the Federal Reserve, or a financial institution doing business in this state.
 - e) repurchase agreements and reverse repurchase agreements shall be entered into only with dealers who have executed a Master Repurchase Agreement with the City.
- 2. In this section, "repurchase agreement" means a simultaneous agreement to buy, hold for a specified time, and sell back at a future date obligations described by Subsection A, 1,a), at a market value at the time the funds are disbursed of not less than the principal amount of the funds disbursed. The term includes a direct security repurchase agreement and a reverse security repurchase agreement.
- 3. Notwithstanding any other law, the term of any reverse security repurchase agreement may not exceed 90 days after the date the reverse security repurchase agreement is delivered.
- 4. Money received by an entity under the terms of a reverse security repurchase agreement shall be used to acquire additional authorized investments, but the term of the authorized

investments acquired must mature no later than the expiration date stated in the reverse security repurchase agreement.

D. Banker's Acceptances

- 1. A banker's acceptance is an authorized investment under this subchapter if the banker's acceptance:
 - a) has a stated maturity of 270 days or fewer from the date of its issuance;
 - b) will be, in accordance with its terms, liquidated in full at maturity;
 - c) is eligible for collateral for borrowing from a Federal Reserve Bank; and
 - d) is accepted by a bank organized and existing under the laws of the United States or any state, if the short-term obligations of the bank, or of a bank holding company of which the bank is the largest subsidiary, are rated not less that A-1 or P-1 or an equivalent rating by at least one nationally recognized credit rating agency.

E. Commercial Paper

- 1. Commercial paper is an authorized investment under this subchapter if the commercial paper;
 - a) has a stated maturity of 270 days or fewer from the date of its issuance; and
 - b) is rated not less than A-1 or P-1 or an equivalent rating by at least;
 - c) two nationally recognized credit rating agencies; or
 - d) one nationally recognized credit rating agency and is fully secured by an irrevocable letter of credit issued by a bank organized and existing under the laws of the United States or any state.

F. Mutual Funds

- 1. A no-load money market mutual fund is an authorized investment under this subchapter if the mutual fund:
 - a) is registered with and regulated by the Securities and Exchange Commission;
 - b) provides the investing entity with a prospectus and other information required by the Securities and Exchange Act of 1934 (15 U.S.C. Section 80a-1 et seq.);
 - c) has a dollar-weighted average stated maturity of 90 days or fewer; and
 - d) includes in its investment objectives the maintenance of a stable net asset value of \$1 for each share.
- 2. In addition to a no-load money market mutual fund permitted as an authorized investment in Subsection 1, a no-load mutual fund is an authorized investment under this Section if the mutual fund:

- a) is registered with the Securities and Exchange Commission;
- b) has an average weighted maturity of less than two years;
- c) is invested exclusively in obligations approved by this subchapter;
- d) is continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or it equivalent; and
- e) conforms to the requirements set forth in Sections G, 2 and 3 relating to the eligibility of investment pools to receive and invest funds of investing entities.

3. An entity is not authorized by this section to:

- a) invest in the aggregate more than 80 percent of its monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service, in money market mutual funds described in Subsection F, 1 or mutual funds described in Subsection 2, either separately or collectively;
- b) invest in the aggregate more than 15 percent of its monthly average fund balance, excluding bond proceeds and reserves in other funds held for debt service, in mutual funds described in Subsection 2;
- c) invest any portion of bond proceeds, reserves and funds held for debt service, in mutual funds described in Subsection 2; or
- d) invest its funds or funds under its control, including bond proceeds and reserves and other funds held for debt service, in any one mutual fund described in Subsection 1 or 2 in an amount that exceeds 10 percent of the total assets of the mutual fund.

G. Investment Pools

- 1. An entity may invest its funds and funds under its control through an eligible investment pool if the governing body of the entity by rule, order, ordinance, or resolution, as appropriate, authorizes investment in the particular pool. An investment pool shall invest the funds it receives from entities in authorized investments permitted by this subchapter.
- 2. To be eligible to receive funds from and invest funds on behalf of an entity under this chapter, an investment officer or other authorized representative of the entity an offering circular or other similar disclosure instrument that contains, at a minimum, the following information:
 - a) the types of investments in which money is allowed to be invested;
 - b) the maximum average dollar-weighted maturity allowed, based on the stated maturity date, of the pool;
 - c) the maximum stated maturity date any investment security within the portfolio has;
 - d) the objectives of the pool;
 - e) the size of the pool;

- f) the names of the members of the advisory board of the pool and the dates their terms expire;
- g) the custodian bank that will safekeep the pool's assets;
- h) whether the intent of the pool is to maintain a net asset value of one dollar and the risk of market price fluctuation;
- i) whether the only source of payment is the assets of the pool at market value or whether there is a secondary source of payment, such as insurance or guarantees, and a description of the secondary source of payment;
- j) the name and address of the independent auditor of the pool;
- k) the requirements to be satisfied for an entity to deposit funds in and withdraw funds from the pool and any deadlines or other operating policies required for the entity to invest funds in and withdraw funds from the pool; and
- l) the performance history of the pool, including yield average dollar-weighted maturities, and expense ratios.
- 3. To maintain eligibility to receive funds from and invest funds on behalf of an entity under this chapter, an investment pool must furnish to the investment officer or other authorized representative of the entity:
 - a) investment transaction confirmations; and
 - b) a monthly report that contains, at a minimum, the following information:
 - i. the types and percentage breakdown of securities in which the pool is invested;
 - ii. the current average dollar-weighted maturity, based on the stated maturity date, of the pool;
 - iii. the current percentage of the pool's portfolio in investments that have stated maturities of more than one year;
 - iv. the book value versus the market value of the pool's portfolio, using the amortized cost valuation;
 - v. the size of the pool;
 - vi. the number of participants in the pool;
 - vii. the custodian bank that is safekeeping the assets of the pool;
 - viii. a listing of daily transaction activity of the entity participating in the pool;
 - ix. the yield and expense ratio of the pool;
 - x. the portfolio managers of the pool; and

- xi. any changes or addenda to the offering circular.
- 4. An entity by contract may delegate to an investment pool the authority to hold legal title as custodian of investments purchased with its local funds.
- 5. In this section, "yield" shall be calculated in accordance with regulations governing the registration of open-end management investment companies under the Investment Company Act of 1940, as promulgated from time to time by the Federal Securities and Exchange Commission.
- 6. To be eligible to receive funds from and invest funds on behalf of an entity under this chapter, a public funds investment pool created to function as a money market mutual fund must mark its portfolio to market daily, and, to the extent reasonably possible, stabilize a \$1 net asset value. If the ratio of the market value of the portfolio divided by the book value of the portfolio is less than 0.995 or greater than 1.005, portfolio holdings shall be sold as necessary to maintain the ratio between 0.995 and 1.005.
- 7. To be eligible to receive funds from and invest funds on behalf of an entity under this chapter, a public funds investment pool must have an advisory board composed:
 - a) equally of participants in the pool and other persons who do not have a business relationship with the pool and are qualified to advise the pool, for a public funds investment pool created under Chapter 791 and managed by a state agency; or
 - b) of participants in the pool and other persons who do not have a business relationship with the pool and are qualified to advise the pool, for other investment pools.
- 8. To maintain eligibility to receive funds from and invest funds on behalf of an entity under this chapter, an investment pool must be continuously rated no lower that AAA or AAA-m or at an equivalent rating by at least one nationally recognized rating service.

EXISTING INVESTMENTS Any investments currently held that do not meet the guidelines of this policy shall be reviewed to determine the ability to liquidate. If the investment cannot be liquidated because of material adverse change in the value since the time of purchase, and holding the investment to maturity does not negatively affect disbursements or cash flow, a recommendation of holding said investment to maturity is acceptable.

<u>PROCUREMENT</u> Investments of subsections A-G of this section, excluding new issues, may be made only after competitive bids are solicited from at least three sources.

<u>MONITORING</u> The market value of each investment shall be obtained monthly from a source such as the Wall Street Journal newspaper, a reputable brokerage firm or security pricing service and reported on the monthly investment reports.

<u>LENGTH OF INVESTMENTS</u> The maximum stated maturity, from the date of purchase, for any individual investment may not exceed 5 years and the maximum dollar-weighted average maturity for the pooled fund group (investment portfolio) may not exceed 2 years.

<u>DIVERSIFICATION</u> It is the policy of the City of La Porte to diversify its investment portfolios. Assets held in the common investment portfolio shall be diversified to eliminate the

risk of loss resulting from one concentration of assets in a specific maturity, a specific issuer or a specific class of securities. Diversification strategies shall be determined and revised periodically by the Audit Committee.

In establishing specific diversification strategies, the following general policies and constraints shall apply:

- A. Portfolio maturities shall be staggered in a way that protects interest income from the volatility of interest rates and that avoids undue concentration of assets in a specific maturity sector. Securities shall be selected which provide for stability of income and reasonable liquidity.
- B. The Audit Committee shall establish strategies and guidelines for the percentage of the total portfolio that may be invested in securities other than repurchase agreements, Treasury bill and notes, or insured and collateralized certificates of deposits. The Audit Committee shall conduct a semi-annual review of these guidelines, and shall evaluate the probability of market and default risk in various investment sectors as part of its considerations.

VII. SELECTION OF BANKS AND DEALERS

<u>BIDDING PROCESS</u> Depositories shall be selected through the City's banking services procurement process, which shall include a formal request for proposal (RFP) issued every two (2) years. In selecting depositories, the credit worthiness of institutions shall be considered, and the Director of Finance shall conduct a comprehensive review of prospective depositories credit characteristics and financial history.

<u>INSURABILITY</u> Banks and Savings & Loans Associations seeking to establish eligibility for the City's competitive certificate of deposit purchase program, shall submit financial statements, evidence of Federal insurance and other information as required by the Director of Finance.

PRIMARY DEALERS AND APPROVED LIST For brokers and dealers of government securities, Investment Officials shall select only those dealers reporting to the Market Reports Division of the Federal Reserve Bank of New York, also known as "primary government securities dealers," unless a comprehensive credit and capitalization analysis reveals that other firms are adequately financed to conduct public business. Before engaging in investment transactions with a broker/dealer, the Investment Official shall have received, from a Qualified Representative of said firm, a signed Certification Form. (Exhibit B) This form shall attest that the individual responsible for the City's account with that firm has reviewed the City's Investment Policy and that the brokerage firm has implemented reasonable procedures and controls in an attempt to preclude imprudent activities arising out of investment transactions conducted between the City and the brokerage firm. The audit committee shall at least annually review, revise, and adopt a list of qualified brokers that are authorized to engage in investment transactions with the City. (Exhibit A)

VIII. SAFEKEEPING AND CUSTODY

<u>INSURANCE OR COLLATERAL</u> All bank deposits, certificates of deposit, and repurchase agreements shall be secured by pledged collateral. Bank deposits and certificates of deposit shall be collateralized with a market value equal to no less than 102% of the deposits plus accrued interest less than an amount insured by FDIC. Repurchase agreements shall be monitored daily. Evidence of the pledged collateral shall be maintained by the Director of

Finance or a third party financial institution. Repurchase agreements shall be documented by specific agreement noting the collateral pledged in each agreement. Collateral shall be reviewed monthly to assure the market value of the securities pledged equals or exceeds the related bank balances.

<u>SAFEKEPING AGREEMENT</u> All safekeeping arrangements shall be in accordance with a Safekeeping Agreement approved by the Audit Committee which clearly defines the procedural steps for gaining access to the collateral should the City of La Porte determine that the City's funds are in jeopardy. The safekeeping institution, or Trustee, shall be the Federal Reserve Bank or an institution not affiliated with the firm pledging the collateral. The safekeeping agreement shall include the signatures of the City of La Porte, the firm pledging the collateral, and the Trustee.

<u>COLLATERAL DEFINED</u> The City of La Porte shall accept only the following securities as collateral:

- A. FDIC insurance coverage;
- B. United States Treasuries and Agencies;
- C. Texas State, City, County, School or Road District bonds with a remaining maturity of ten (10) years or less with rating from a nationally recognized investment rating firm and having received a rating of not less than A or its equivalent;
- D. Other securities as approved by the Audit Committee.

<u>SUBJECT TO AUDIT</u> All collateral shall be subject to inspection and audit by the Director of Finance or the City's independent auditors.

<u>DELIVERY VERSUS PAYMENT</u> Treasury Bills, Notes & Bonds and Government Agencies' securities shall be purchased using the delivery versus payment method. That is, funds shall not be wired or paid until verification has been made that the collateral was received by the Trustee. The collateral shall be held in the name of the City or held on behalf of the City. The Trustee's records shall assure the notation of the City's ownership of or explicit claim on the securities. The original copy of all safekeeping receipts shall be delivered to the City.

IX. MANAGEMENT AND INTERNAL CONTROLS

The Director of Finance shall establish a system of internal controls, which shall be reviewed by an independent auditor. The controls shall be designed to prevent losses of public funds arising from fraud, employee error, misrepresentation by third parties, unanticipated changes in financial markets, or imprudent actions by employees or Investment Officials of the City.

Controls and managerial emphasis deemed most important that shall be employed where practical are:

- A. Control of collusion.
- B. Separation of duties.
- C. Separation of transaction authority from accounting and record keeping.

- D. Custodian safekeeping receipts records management.
- E. Avoidance of bearer-form securities.
- F. Clear delegation of authority.
- G. Documentation on investment bidding events.
- H. Written conformation of telephone transactions.
- I. Reconcilement and comparisons of security receipts with the investment subsidiary records.
- J. Compliance with investment policies.
- K. Accurate and timely reports.
- L. Validation of investment maturity decisions with supporting cash flow data.
- M. Adequate training and development of Investment Officials.
- N. Verification of all interest income and security purchase as sell computations.
- O. Review of financial condition of all brokers, dealers and depository institutions.
- P. Staying informed about market conditions, changes, and trends that require adjustments in investment strategies.

COMPLIANCE AUDIT The City of La Porte shall perform, in conjunction with its annual financial audit, a compliance audit of management controls on investments and adherence to the entity's established investment policies. The audit shall include a formal review of the quarterly investment reports by an independent auditor and the results reported to the governing body by the independent auditor. Also, the governing body shall review its investment policy and investment strategy not less than annually and adopt a written instrument by rule, order, ordinance, or resolution stating that it has reviewed the investment policy and strategy, and recorded any changes made to them.