

THE CITY OF GALVESTON

INVESTMENT POLICY

XXXXXXXX 2020

(City Council Approved XXXXXXXXXXXX NN, 2020 Item XX.X)



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Investment Policy
City of Galveston, Texas

Policy Statement

The Investment Policy, known as “The Investment Policy of the City of Galveston” (the “Investment Policy”) complies with and incorporates the Public Funds Investment Act, (the “Act”), Chapter 2256, Texas Government Code and the Public Funds Collateral Act, Chapter 2257, Texas Government Code.

All applicable provisions of the Act, as amended, are adopted by incorporation of Appendix A, the Act, in its entirety.

In the event of a conflict with these investment policies and the Act, the more restrictive of the two shall control.

All participants in the investment process shall act responsibly as custodians of the public trust.

It is the policy of the City of Galveston (the “City”) that the administration and investment of its funds shall be handled as its highest public trust. Investments shall be made in a manner which will provide the maximum security of principal through risk management and diversification while meeting the daily cash flow needs of the City and conforming to all applicable state and local statutes, rules and regulations governing the investment of public funds.

The Investment Policy is based on standards of prudent money management. Effective cash flow management and cash investment practices are recognized as essential to good fiscal management and have been incorporated into the investment program.

I. Scope

The Investment Policy shall apply to all financial assets and pooled funds of the City and govern the management of Investments by the Finance Department of the City of Galveston. The Investment Policy shall govern the investment management process with respect to investments managed by the Finance Department of the City of Galveston for the General Fund, Special Revenue Funds, Debt Service Funds, Capital Project Funds and Enterprise Funds. The investments will meet the cash flow requirements of the City as established by City Council and City management. These funds are defined in the City’s Comprehensive Annual Financial Report (CAFR). This Investment Policy applies to any new fund created by the City unless specifically exempted by the City Council and this Investment Policy.

II. General Objectives

(1) The emphasis of all investment activity shall be safety, liquidity, diversification and yield.

- a. **Safety.** The primary objective shall be on safety and preservation of principal. Adherence to the permitted investments listed in the Investment Policy will maximize safety. Whenever practical, assets held in the common investment portfolio shall be diversified to minimize the risk of loss resulting from one concentration of assets in a specific maturity, a specific issuer, or a specific class of securities. Whenever possible, the City will purchase non-callable securities in order to best ensure the laddering of maturities and balancing of classes of securities. The City's investments shall be reviewed and rebalanced with respect to diversification at least once per calendar quarter. The emphasis shall be on maintaining a prudent level of cash (money market and investment pool) balances, relative to security types and maturities.
- b. **Liquidity.** The goal of liquidity is to maintain available cash balances sufficient to cover anticipated and unexpected cash demands. The City's investment portfolio will remain sufficiently liquid to meet all daily operating requirements.
- c. **Diversification.** Whenever practical, assets held in the portfolio(s) shall be diversified to minimize the risk of loss resulting from the concentration of assets in a specific maturity, a specific issuer, or a specific market sector. The City's investments shall be reviewed and rebalanced with respect to diversification at least once per calendar quarter.
- d. **Yield.** Yield considerations shall be subordinate to safety and liquidity requirements, but shall be maximized within those constraints through prudent and active management.

(2) **Loss of Required Ratings.** The Investment Officers shall take all prudent measures consistent with this Investment Policy to liquidate an investment that does not meet any minimum specified rating. Investment Officers or the Advisor will monitor the credit ratings of all rated investments at all times. Should any investment requiring minimum ratings be placed on market watch, downgraded or placed on credit watch by any nationally recognized rating agency, Investment Officers shall notify the Finance Director immediately. Liquidation of the security may, but need not be, effected. Evaluation of the cause of the action, the maturity of the security, and the position of the security in the portfolio will be considered and prudent measures taken to protect City funds.

(3) **Prudent Person Rule.** The standard of prudence to be used in the investment function shall be the "prudent person" standard and

shall be applied in the context of managing the overall portfolio. This standard states:

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

In determining whether investment personnel exercised prudence with respect to an investment decision, the determination shall be made taking into consideration:

- a. the investment of all funds over which investment personnel had responsibility rather than a consideration as to the prudence of a single investment, and
- b. whether the investment decision was consistent with the written Investment Policy.

Investment personnel involved in investment decisions, when acting in accordance with this Investment Policy and exercising due diligence, shall not be held responsible for a change in a specific investment's credit risk or market price, provided deviation from expectations are reported in a timely manner and appropriate action is taken to control adverse developments.

III. Investment Strategy

The City commingles its operating and reserve funds into one investment portfolio for investment purposes of efficiency, accurate distribution of interest, and maximum investment opportunity. Bond funds are managed separately in accordance with their anticipated expenditure schedule. Although commingled, the City recognizes the unique characteristics and needs of the individual funds in its strategy statement and management of the funds. The maximum dollar weighted average maturity of the entire portfolio shall be no greater than 18 months.

- (1) **Operating Funds.** The investment strategy for operating funds has as its primary objective assurance that anticipated liabilities are matched and adequate investment liquidity provided. This may be accomplished by purchasing high quality, short- to medium-term maturity securities, which will complement each other in a laddered maturity structure permitting some extension for yield enhancement.
- (2) **Debt Service Funds.** The investment strategy for debt service funds shall have as its primary objective the assurance of available funds adequate to fund the debt service obligations on a timely

basis. Successive debt service dates will be fully funded before extension.

- (3) **Bond Reserve Funds.** The investment strategy for bond reserve funds shall have as its primary objective the ability to generate a revenue stream to the bond reserve funds from high quality securities with a low degree of volatility. Securities should be high credit quality and, except as may be required by a bond ordinance specific to an individual issue, of short to intermediate-term maturities. Reserve portfolios will utilize securities with a maximum maturity of five years and have a maximum weighted average maturity, if managed as a separate portfolio, not to exceed three years.
- (4) **Capital Project Funds.** The investment strategy for capital project funds will have as its primary objective assurance that anticipated expenditures are matched with maturing investments for adequate liquidity. The stated final maturity dates of securities held may not exceed the estimated project completion date.

Separately managed portfolios are to be managed with the specific expenditure schedules and legal requirements of those funds. The portfolios will be guided by the provisions of this Investment Policy.

Cash Management

Effective cash management is recognized as essential to a prudent investment strategy and overall fiscal management. Cash management is defined as the process of managing monies in order to ensure maximum cash availability and use. The City shall maintain a comprehensive cash management program, which includes collection of accounts receivable, prudent investment of its available cash, disbursement of payments in accordance with invoice terms and the management of banking services.

As a part of this comprehensive cash management program, the City recognizes that there is the potential need for unexpected cash drawdowns during the hurricane season which commences in June and concludes in November of each year. The portfolio should be structured so that adequate investments mature during this period.

IV. Suitable and Authorized Investments

Authorized investments shall be limited to the following, as further defined by the Act:

- (1) Obligations of the United States or its agencies and instrumentalities to include obligations in which the principal and interest 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, including obligations that are fully

guaranteed or insured by the Federal Deposit Insurance Corporation (“FDIC”), National Credit Union Share Insurance Fund (“NCUSIF”) or by the explicit full faith and credit of the United States per Texas State Code 2256.009.

- (2) Obligations of the Federal Home Loan Bank (FHLB) per Texas State Code 2256.009.
- (3) Municipal Securities per Texas State Code 2256.009
- (4) Fully insured or collateralized certificates of deposit at commercial banks, savings banks and credit unions per Texas State Code 2256.010.
- (5) Repurchase agreements collateralized by U.S. Treasury or U.S. Government Agency securities per Texas State Code 2256.011
- (6) Securities and Exchange Commission (the “SEC”) registered, no load money market funds as permitted by Texas State Code 2256.014.
- (7) Texas local government investment pools per Texas State Code 2256.016. Although this Investment Policy does not permit direct purchase of commercial paper, investment pools that contain commercial paper as well as any investment specifically authorized within the Act are permitted.

The City’s ownership share of any public funds investment pool shall be limited to 10% of the overall pool balance.

Exemption of Existing Investments

The City is not required to liquidate investments that were authorized investments at the time of purchase. Any investments held that do not meet the guidelines of the Investment Policy shall be reviewed to determine ability to liquidate. If the security cannot be liquidated because of material adverse changes in value since the time of purchase, and holding the security to maturity does not negatively affect disbursement or cash flow, a recommendation of holding the security to maturity is acceptable. At all times, liquidations shall be effected taking into account the prudent person standard.

Certain Prohibited Investments

The City is prohibited from investing in companies that do business in Sudan, Iran, or with Foreign Terrorist Organizations (collectively known as “Listed Companies”).

V. Incorporation of the Public Funds Investment Act

- (1) **Competitive Bidding.** All individual security transactions shall require at least three competitive bids/offers where practicable.
- (2) **Delivery versus Payment.** Transactions must be settled on a delivery-versus-payment (DVP) basis to a City approved depository except for transactions involving mutual funds or investment pool

funds. This assures City control of all its funds and assets. No securities shall be held by transaction counterparty.

(3) **Independent Third-Party Safekeeping.** Collateral provided for bank time and demand deposits as well as repurchase agreements will be held by an independent third-party safekeeping agent approved by the City and providing the City with original safekeeping receipts. Authorized collateral will include:

- a. Obligations of the U.S. Government and its agencies and instrumentalities, including mortgage-backed securities.
- b. Municipal obligations of any state or subdivision, rated no less than AA or equivalent by a Nationally Recognized Statistical Rating Organization (“NRSRO”).

All City-owned securities will be registered and held in the name of the City in a segregated third-party safekeeping account through the City’s contracted depository. Financial institutions serving as City depositories will be required to sign a tri-party depository agreement with the City and the independent safekeeping agent (custodian) in compliance with the Financial Institutions reform, Recover, and Enforcement Act (“FIRREA”). The agreement shall define the collateral and City rights to the collateral in case of default, bankruptcy, or closing and shall establish a perfected security interest in compliance with Federal and State regulations, which require that:

- a. The Agreement be in writing;
- b. The Agreement be approved by the Board of Directors or the Loan Committee of the Depository and a copy of the meeting minutes or resolution reference must be delivered to the City; and
- c. No listing of pledged collateral shall be part of the written agreement.

(4) **Collateral Policy.** Collateralization is required for all uninsured collected balances. Collateral will be equal to or exceed 110% of the total deposit amount of all operating accounts, with accrued interest, if any. Substitution will be granted with prior City approval. Counterparties will be contractually liable for monitoring and maintaining the required margin levels on all collateral at all times. The City will value the collateral securities monthly unless market conditions warrant more frequent valuation. If the market value of collateral is deficient, additional collateral must be requested.

Collateral will be equal to or exceed 102% of the daily repurchase sweep agreement amount.

VI. Diversification and Maximum Maturities

(1) **Diversification.** Diversification will be used to minimize risk of loss by over-investment in a particular market sector, maturity or security. The City will strive for portfolios with laddered maturities and securities in accordance with the authorized investments and maximum maturity constraints. To assure diversification in the portfolio the following limits will be imposed:

| <u>Investment Type</u> | <u>Max. % in Portfolio</u> |
|--|----------------------------|
| US Treasury Obligations | 100% |
| US Agency and Instrumentality Obligations | 80% |
| SEC Registered Money Market Funds | 50% |
| Repurchase Agreements | 50% |
| Flex Repurchase (Bond Funds) | 50% |
| Municipal Securities | 20% |
| Local Government Investment Pools | 100% |
| Collateralized, FDIC or NCUSIF-insured CDs | 50% |

(2) **Maximum Maturities.** The maximum maturity for investments designated for operations, current debt service, and construction funds shall not exceed 36 months. The maturity for debt service reserve holdings can be extended to the life of the bond maturity or five years, whichever is less.

(3) **Weighted Average Maturity for Pooled Fund Groupings.** The maximum dollar weighted average maturity of the entire portfolio shall be no greater than 18 months based on the stated maturity date.

VII. Finance, Fiscal Affairs and Investment Advisory Committee (the “Committee”)

Ordinance No. 19-042 established the reconstituted Finance and Fiscal Affairs Committee which is now charged with the duties of the Investment Advisory Committee. The committee shall be composed of seven voting members, and one non-voting ex-officio member of city council. All members shall be appointed by the city council. There shall be appointed additional non-voting, advisory members as deemed necessary and as appointed by the city council.

The committee is established to review and evaluate for the purpose of making recommendations to council, review of the city’s financial statements and reports, audit, budget and budget performance, fund accounting and fund balances, and financial management policies. The Committee’s responsibilities also include the review of the City’s Investment Policy annually, review investment recommendations, review investment reports, oversee the City’s investment portfolio to ensure compliance with State law, adopt a list of qualified brokers authorized to engage in investment

transactions and approve the independent source providing state mandated investment training.

VIII. Designation of Investment Officers

- (1) **Delegation of Investment Authority.** The Assistant City Manager of Finance, Executive Director/City Controller and Accounting Manager shall be designated as Investment Officers to execute the investment management process of local revenues. Investments of five (5) million or more will require authorization by two investment officers. The Assistant City Manager of Finance may temporarily designate another qualified staff individual to function as Investment Officer in his or her place if and when necessary. That individual will also attend the state mandated training described below.

The Investment Officers shall review investment positions at least once per quarter for conformance to this Investment Policy and the needs of the City.

The Investment Officers shall develop and maintain written administrative procedures for the operation of the investment program, which are consistent with this Investment Policy. Procedures will include safekeeping, settlement, documentation, agreements, contracts, and other investment related activities.

- (2) **Investment Training.** The Investment Officers shall attend ten (10) hours of investment training within twelve (12) months of assuming duties, and subsequently shall attend 10 hours of training within every succeeding two-year period following the initial 10 hours of training completed within the first 12 months of assuming duties, as required by the Act. The training cycle becomes concurrent with the City's fiscal year.

The training sessions shall be provided by the Texas Municipal League, the Government Finance Officers Association of Texas (GFOAT), the Government Treasurers Organization of Texas (GTOT), the University of North Texas Center for Public Management, the Texas Society of Certified Public Accountants, or any other independent source approved by the Committee.

Training must include education in investment controls, security risks, strategy risks, market risks, diversification of investment portfolio, and compliance with PFIA.

Capability of Investment Management. Professional services may be used to provide expertise in the areas of Investments, cash management, bonded indebtedness, and other areas deemed appropriate by City Council and the Executive Management Team

(EMT). The EMT addresses quality and capability of investment management through the utilization of State laws pertaining to these services. These services shall be subordinate to City Management and this Investment Policy, as applicable.

The City may contract with an Investment Advisor, who shall adhere to the spirit, philosophy and specific term of this Investment Policy and shall invest within the same standard of prudence. The Investment Advisor must be registered with the SEC under the Investment Advisor's Act of 1940 as well as with the Texas State Securities Board. Advisors may assist the City with the management of its funds and other responsibilities including, but not limited to: review of investment policy, development of appropriate investment strategies, security analysis, trade execution, security clearance, broker dealer compliance, investment reporting and security documentation.

- (3) **Ethics Disclosure and Conflicts of Interest.** If an Investment Officer has a personal business relationship as defined in the Act, with a business organization engaging in investment transactions with the City or, the officer is related within the second degree by affinity or consanguinity to an individual seeking to transact with the City, the Investment Officer must disclose the relationship and file a disclosure with the City Secretary and the Texas Ethics Commission.

IX. Establishment and Annual Review of Qualified Bidders list

Investments shall be executed through broker/dealers and/or banks only. The Committee will review, revise and approve the list of authorized broker/dealers annually. The Investment Officers or investment advisor will obtain and maintain information on each authorized broker/dealer.

Securities broker/dealers must meet certain criteria as determined by the Investment Officers. The following criteria must be met by firms on the list:

- provision of an audited financial statement for the most recent period,
- proof of registration with the Financial Industry Regulatory Authority (FINRA), and
- proof of current registration with the Texas State Securities Commission.

If the City has contracted with an Investment Advisor, the Advisor shall be responsible for performing due diligence on broker/dealers and shall provide a list of approved broker/dealers to the City no less than annually. The Investment Advisor shall meet the requirements of Texas State Code 2256.003.

X. Investment Policy Certification

The City shall present a copy of this Investment Policy to any business organization offering to engage in an investment transaction with the City. An authorized representative of an investment pool or Investment Advisory firm acting in a discretionary capacity shall execute a Policy Certification form substantially to the effect that the representative has received and thoroughly reviewed the Investment Policy, and acknowledged that the organization has implemented reasonable procedures and controls in an effort to preclude investment transactions that are not authorized by this Investment Policy, except to the extent that the authorization is dependent on an analysis of the makeup of the City's primary commingled portfolio or requires an interpretation of subjective investment standards.

XI. Investment Reporting

Quarterly Reporting. The Investment Officers and Investment Advisor shall provide to City Council, not less than quarterly, a written report of investment positions and activity in accordance with Section 2256.023 of the Act.

Marking to Market. The quarterly investment report shall include the market value of the portfolio. Market values shall be obtained from the Investment Advisor or other independent sources such as a safekeeping institution or industry publications. If market values are unavailable from independent sources, the City may obtain market values from its authorized brokers, provided the broker providing the market price is not the same broker that sold the security to the City. The market price of investments acquired with public funds is monitored by a third party Investment Advisor firm (engaged by the City) with access to pricing applications (e.g. Bloomberg).

XII. Internal Controls

The Assistant City Manager of Finance shall establish a system of internal controls designed to prevent losses due to fraud, employee error, negligence, collusion, third party misrepresentation, and unanticipated market changes as well as other foreseeable circumstances arising in the investment function. The controls are to safeguard City assets and securities throughout the investment process. The internal control structure shall be designed to provide reasonable assurance that these Investment Policy objectives are met and controls shall be reviewed annually with the independent auditor of the City.

Transactions shall, in all cases, comply with established internal controls especially as regards the transfer of funds.

The concept of reasonable assurance recognizes that:

- a. The cost of a control should not exceed the benefits likely to be derived, and
- b. The valuation of costs and benefits requires estimates and judgments by management.

The controls shall address, at a minimum, the functions of documentation; competitive bidding practices; delivery and custody of securities; perfected ownership; collateralization; timely reconciliation of transactions, receipts and statements; required audits; and financial counter-parties. The controls shall address these functions with attention to potential collusion, separation of duties, and clear delegation of authority.

XIII. Review by Independent Auditor

The City's audit engagement shall include a compliance audit of management controls on investments and adherence to the City's established investment policies. The compliance audit shall be performed annually in conjunction with the City's financial audit and will include a review of the quarterly reports.

XIV. Annual Review and Adoption of Investment Policy and Strategies

The City Council of the City of Galveston shall review and adopt this Investment Policy and its incorporated investment strategies not less than annually. The approving resolution will list all changes being made to the Policy.

Appendix A – Texas Government Code 2256

PROPOSED

Attachment A - Policy Certification

PROPOSED



PROPOSED