

RFP# 15-020: Investment Advisory Services
Attachment A



**City of Round Rock, Texas
Investment Policy & Strategy
October 9, 2014**

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City of Round Rock, Texas
Investment Policy
October 9, 2014

"I'm not as concerned about the return on my principal as I am about the return of my principal."

Will Rogers

I. Introduction

The Investment Policy of the City of Round Rock, Texas, is adopted in accordance with Chapter 2256, Texas Government Code, the Public Funds Investment Act (the "Act"). This Policy establishes guidelines for the Investment Officers with regard to how City funds will be invested. This Policy also establishes guidelines for periodic review and reporting of the investments.

II. Scope And Legal Requirements

A. Scope

This Investment Policy for the City of Round Rock, Texas applies to the financial assets of all funds, including the following City funds:

- 1) General Fund
- 2) Special Revenue Funds
- 3) Debt Service Funds
- 4) Capital Project Funds
- 5) Enterprise Funds
- 6) Internal Service Funds
- 7) Trust and Agency Funds
- 8) Reserve Fund
- 9) Any new funds created by the City and any funds managed by the City of Round Rock, Texas, as trustee or agency, unless exempted by law. In addition to this Policy, bond

funds established by bond ordinances shall be managed by their governing ordinances and all applicable State and Federal Law.

B. State Statute

All funds covered by this Investment Policy shall be invested in accordance with the Public Funds Investment Act as amended from time to time. (Texas Government Code, Ch. 2256.)

C. Delegation of Authority

The Director of Finance, the Assistant Finance Director, the Accounting Manager, and the Treasury Accountant are hereby designated as the Investment Officers of the City of Round Rock, Texas, and are responsible for investment decisions and activities consistent with this Investment Policy.

The Investment Officers shall be responsible for all transactions and compliance with the internal controls, insure all safekeeping, custodial, and collateral duties consistent with this Investment Policy, as well as establishing and maintaining written procedures for cash management. The Investment Officers shall maintain timely, accurate and systematic records of all investments, maturities and earnings. Bonding of all staff with financial signatory authority is required and such bonding requirements will also apply to those individuals authorized to place, purchase or sell investment instruments. Bonding will protect the public against loss from possible embezzlement and malfeasance.

III. Investment Objectives

A. Safety of Principal

The primary objective of all investment activity is the preservation of capital and the safety of principal in the overall portfolio. Each investment transaction shall seek to ensure first that capital losses are avoided, whether they have resulted from securities defaults or erosion of market value.

With foremost emphasis on safety of principal (i.e. avoidance of capital losses), the Investment Officers will ensure that preservation of capital and protection of principal in the overall portfolio is maintained. Speculation is prohibited.

B. Maintenance of Adequate Liquidity

The investment portfolio will remain sufficiently liquid to meet the cash flow requirements that might be reasonably anticipated. Liquidity shall be achieved by matching investment maturities with anticipated cash flow requirements; investing in securities with active secondary markets; and maintaining appropriate portfolio diversification.

IV. Standard of Care

Investments shall be made with judgment and care, under prevailing circumstances, that a person of prudence, discretion and intelligence would exercise in the management of the person's own affairs, not for speculation, but for investment, considering the probable safety of capital and the probable income to be derived. The standard of care shall be applied to the context of managing the overall portfolio.

V. Investment Strategy

In conjunction with the annual Policy review, the City Council shall review the separate written investment strategy for each of the City's funds. The investment strategy must describe the investment objectives for each particular fund according to the following priorities:

- 1) Investment suitability
- 2) Preservation and safety of principal
- 3) Liquidity
- 4) Marketability prior to maturity of each investment
- 5) Diversification
- 6) Yield

VI. Authorized Investments

A. Authorized Investments

The following is a list of authorized and legal investment options:

- 1) Obligations of the United States or its agencies and instrumentalities, excluding mortgage backed securities, with a maximum stated maturity of three (3) years);
- 2) Direct obligations of the State of Texas or its agencies and instrumentalities with a maximum stated maturity of three (3) years);
- 3) Other obligations the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, the State of Texas or the United States or

their respective agencies and instrumentalities with a maximum stated maturity of three (3) years);

4) 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 with a maximum stated maturity of three (3) years) .

5) Certificates of Deposit as authorized under the Act with a maximum maturity of two years.

6) Repurchase Agreements which are fully collateralized as authorized by the Act. Flex repurchase agreements may be used for capital project funds but will not extend past the anticipated expenditure schedule.

7) A1/P1 Commercial Paper as authorized by the Act with a maximum maturity of 90 days.

8) AAA-Rated Money Market Mutual Funds as authorized by the Act, which strive to maintain a \$1 NAV.

9) Constant dollar local government investment pools as authorized by and compliant with the Act.

10) FDIC insured *Brokered Certificate of Deposit* securities purchased from a broker or a bank in Texas, delivered versus payment to the City’s safekeeping agent, not to exceed one year to maturity. Before purchase, the Investment Officer must verify before purchase the FDIC status of the bank on www.2fdic.gov/idasp/main_bankfind.asp to assure that the bank is FDIC insured.

11) Fully insured or collateralized interest bearing accounts from any bank in Texas.

B. Unacceptable Investments

This Policy bestows the authority upon the Investment Officer to determine certain investment instruments as unsuitable for the City even though those investments may be authorized by this Policy and/or the Public Funds Investment Act. Additionally, certain investments are expressly prohibited by the Public Funds Investment Act.

An investment that requires a minimum rating under this Policy and/or the Public Funds Investment Act does not qualify as an authorized investment during the period the investment does not have the minimum rating. The City shall take all prudent measures that are consistent with its Investment Policy to liquidate an investment that does not have the minimum rating.

The Investment Officer shall monitor, on no less than a monthly basis, the credit rating on all authorized investments in the portfolio based upon independent information from a nationally recognized rating agency. If any security falls below the minimum rating required by Policy, the Investment Officer shall immediately solicit bids for and sell the security, if possible, regardless of a loss of principal.

The Investment Officer shall monitor, on no less than a monthly basis, the status and ownership of all banks issuing brokered CDs owned by the city based upon information from the FDIC. If any bank has been acquired or merged with another bank in which brokered CDs are owned, the Investment Officer shall immediately contact the banks and liquidate any brokered CD which is above the FDIC insurance level.

C. Protection of Principal

The City shall seek to control the risk of loss due to the failure of a security issuer or grantor. Such risk shall be controlled by investing only in the safest types of securities as defined in this Policy; by qualifying the broker, dealer and financial institution with whom the City will transact; by collateralization as required by law; and through portfolio diversification by maturity and type.

The purchase of individual securities shall be executed “delivery versus payment” through the City’s safekeeping agent. By so doing, City funds are not released until the City has received, through the safekeeping agent, the securities purchased.

D. Diversification by Investment Type

Diversification by investment type is primarily intended to reduce the credit risk inherent to a particular issuer or investment type. The City will diversify its investments by security type and institution. With the exception of U.S. Treasury securities and authorized pools, and the percentage limitations listed below, no more than 50% of the City’s total investment portfolio will be invested in a single security type or with a single financial institution.

<u>Investment Type</u>	<u>Portfolio Limitation</u>
1) U.S. Government Agencies and Instrumentalities	50%
2) States and their Agencies, Counties, Cities and Other Political Subdivisions of a State.....	35%
3) Commercial Paper	10%
% of any one (1) issuer	5%
4) Money Market bank accounts	30%
5) Depository Certificates of Deposit	15%
6) Brokered Certificats of Deposit	10%

Bond proceeds may be invested in a single security or investment if the Investment Officers determine that such an investment is necessary to comply with Federal arbitrage restrictions or to facilitate arbitrage recordkeeping and calculation.

E. Diversification by Investment Maturity and Weighted Average Maturity

In order to minimize risk of loss due to interest rate fluctuations, investment maturities will not exceed the anticipated cash flow requirements of the funds. The weighted average maturity will be determined on a total portfolio basis with a maximum of 540 days.

Maturity guidelines by fund are as follows:

1) Pooled Funds

Pooled Funds are a pooling of operating funds needed for day to day operations along with special revenue funds, internal service funds, and any other funds that do not fall into one of the three (3) categories listed below.

Maturity Limitation: The maximum allowable maturity shall be three (3) years.

2) Capital Project Funds

Maturity Limitation: Funds used for construction programs have reasonably predictable draw down schedules. Therefore, investment maturities shall generally follow the anticipated cash flow requirements. Bond proceeds (excluding reserve and debt service funds) shall generally be limited to the cash flow requirements or the “temporary period” as defined by Federal tax law. During the temporary period bond proceeds may be invested at an unrestricted yield. After the expiration of the temporary period, bond proceeds subject to yield restriction shall be invested considering the anticipated cash flow requirements of the funds and market conditions to achieve compliance with the applicable regulations.

3) Debt Service Funds

Debt Service Funds shall be invested to ensure adequate funding for each consecutive debt service payment.

Maturity Limitation: The Investment Officers shall invest in such a manner as not to exceed an “unfunded” debt service date with the maturity of any investment. An unfunded debt service date is defined as a coupon or principal payment date that does not have cash or investment securities available to satisfy said payment.

4) Debt Service Reserve Funds

Market conditions, Bond Ordinance constraints and Arbitrage regulation compliance will be considered when formulating Reserve Fund strategy.

Maturity Limitation: Maturities shall generally not exceed the call provisions of the Bond Ordinance and shall not exceed the final maturity of the bond issue. All Debt Service Reserve Fund investment maturities shall not exceed three years.

City funds that are considered “bond proceeds” for arbitrage purposes will be invested using a more conservative approach than the standard investment strategy when arbitrage rebate rules require refunding excess earnings. All earnings in excess of the allowable arbitrage earnings will be made available for any necessary payments to the U.S. Treasury.

VII. Relationships With Financial Institutions and Firms

A. Depositories

Depositories shall be selected through the banking service procurement process, which shall include a formal request for proposals no less than every five (5) years. In selecting the depository, the creditworthiness of institutions shall be considered and the Investment Officers shall conduct a comprehensive review of prospective depositories' credit characteristics and financial history. The City depository contract and other financial relationships for banking services are outside the scope of this Investment Policy.

B. Selection and Compliance of Investment Providers

An investment firm offering to engage in an investment transaction with the City must execute a written instrument stating that the qualified representative has received and thoroughly reviewed the Investment Policy of the City. The qualified representative also must acknowledge that the firm has implemented reasonable procedures and controls to preclude transactions conducted between the City and the firm that are not authorized by the City’s investment policy, except to the extent that this authorization is dependent on an analysis of the makeup of the City’s entire portfolio, or requires an interpretation of subjective investment standards.. The Investment Officers may not acquire or otherwise obtain any authorized investment from a person who has not delivered to the City an instrument in substantially the form described above. The following institutions or firms may qualify under this section:

- 1) Security Dealers which are the approved and designated Dealers of the Federal Reserve Bank of New York "Primary Dealers" and approved by City Council.
- 2) Security Dealers and Brokers which are not designated as "Primary Dealers" but which are approved individually by the City Council.

- 3) Banks domiciled in the State of Texas (for the placement of insured and collateralized certificates of deposit and money market accounts) which need not be formally designated by the City Council.

Addendum A is the list of brokers/dealers who have qualified and are hereby approved to conduct business with the City as required by the Act. The qualified broker/dealer list must be reviewed and approved by City Council at least annually.

VIII. Safekeeping and Custody

To protect against potential fraud and embezzlement, investments shall be secured through third party custody and safekeeping procedures.

Safekeeping of City Owned Securities

All security purchases and trades conducted for the City of Round Rock will be settled and protected by the City's contracted third party safekeeping agent. The use of the Delivery Versus Payment (DVP) procedure will be continually used for investment securities transactions, purchases and sales. The City shall authorize the release of funds only after its safekeeping agent has received securities or receipt for same into the City's safekeeping account.

Securities owned by the City under repurchase agreements shall be secured by written City agreement and all securities will be moved on a DVP basis.

Custody of Pledged Securities

The City shall approve all third party custodial agents for the custody of securities pledged to the City as collateral to secure demand or time deposits purchased as investments.

Safekeeping and custody procedures shall be reviewed annually by the independent auditor.

IX. Depository and Contractual Trading Requirements

A. Wire Transfer Authorizations

Whenever possible, the City will use pre-formatted wire transfer to restrict the transfer of funds to pre-authorized accounts only. Dual authorization forms shall be in continual use for all wire transfers. Secondary authorization for all wires will be required by the City.

B. Collateralization Requirement

The City, in accordance with state statute, requires all City funds held by financial institutions above the FDIC insurable limit to be collateralized with securities pledged to the City. Those securities shall have a market value equaling at least 102% of the total value of City funds held and shall be placed with a third party custodial agent. *Collateral may be substituted or released*

only with the written authorization of an Investment Officer. Allowable collateral may consist only of the following securities as permitted under the Public Funds Collateral Act (Texas Government Code, Ch. 2257).

- Obligations of the US Government, its agencies and instrumentalities including mortgage backed securities and CMOs which pass the *bank test, as defined by the Federal Reserve.*
- Obligations of any US state, agencies, counties, cities and other political subdivisions rated as to investment quality by at least one nationally recognized rating agency.

A monthly report listing the collateral must be provided directly from the Custodian to the City.

Financial institutions serving as City Depositories will be required to sign a Depository Agreement with the City. The “Security for Deposits” portion of the Agreement shall define the City’s 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, including:

1. the Agreement must be in writing
2. the Agreement has to be executed by the Depository and the City contemporaneously with the acquisition of the asset;
3. the Agreement must be approved by the Board of Directors or the Bank Loan Committee of the Depository and a copy of the meeting minutes must be delivered to the City;
4. the Agreement must be part of the Depository’s “official record” continuously since its execution.

X. Portfolio Valuation and Reporting

A. Reporting

As required by law, the Investment Officers shall submit a written investment report, prepared in accordance with GAAP, signed by each Investment Officer of the City within a reasonable time after the end of each fiscal quarter to the City Council detailing the investment position for the previous quarter. Monthly market values will be obtained from the City’s financial advisor, or other source believed to be reliable, in order to monitor the portfolio’s position.

- 1.) For pooled investments -
 - a. the report must state the beginning book value and market value of the pool portfolio for the reporting period,
 - b. changes to the book value and market value during the reporting period
 - c. the ending book value and market value of the portfolio and
 - d. the fully accrued interest for the reporting period.
- 2.) For separately invested assets -

- a. the report must state the book value and market value for each investment at the beginning and end of the reporting period
 - b. the report also must disclose the stated maturity date for each separate investment and must show the specific fund from which moneys were received to purchase the investment.
- 3.) The report must state compliance of the investment portfolio with the City's Investment Strategy and relevant provisions of the Public Funds Investment Act.

B. Internal Controls

The Investment Officers shall establish a system of internal controls, which shall be documented in writing and reviewed periodically by the City auditors. The controls shall be designed to prevent and control losses of public funds arising from fraud, employee error, misrepresentation by third parties, unanticipated changes in financial markets or imprudent actions. Dual controls of all investment activities will consistently be maintained by the Investment Officers.

The Investment Officers shall develop and maintain written administrative procedures for the operation of the investment and cash management program, consistent with this Investment Policy.

C. External Audit

In accordance with the Public Funds Investment Act, in conjunction with the City's annual financial audit, a compliance audit of management controls on investments and adherence to the City's established investment policies shall be performed. An annual review of the City's quarterly reports will also be performed by an independent auditor with the results being presented to the City Council.

XI. Quality and Capability of Investment Management

A. Training

It is the City's policy to provide training required by the Public Funds Investment Act Section 2256.008(a)(2) through courses and seminars offered in compliance with the Act in order to insure the quality and capability of the Investment Officers in making investment decisions.

B. Limitation of Liability

The Investment Officers acting in accordance with this Policy and the City's Investment Strategy and exercising due diligence shall be relieved of personal liability for an individual security's performance provided that deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse development.

C. Ethics

The Investment Officers 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. Furthermore, in accordance with the Public Funds Investment Act, an Investment Officer who has a personal business relationship with a firm or is related to individuals seeking to sell to the Investment Officer must disclose such relationships in accordance with Section 2256.005 of the Public Funds Investment Act.

XII. Review and Amendment

This Policy shall be reviewed and adopted annually by the City Council.

XIII. Conclusion

The Investment Officers will adhere to this Investment Policy in all investment decisions for the City of Round Rock, Texas. The City Council will review and adopt, by resolution, the Investment Policy every year because of the dynamic nature of the financial markets. If changes are necessary because of changes to the financial markets and/or State law, the adopting resolution will include reference to the changes.

City of Round Rock, Texas **Investment Strategy**

In order to minimize risk of loss due to interest rate fluctuations, investment maturities will not exceed the anticipated cash flow requirements of the funds. The investment strategy for all funds is established according to the following priorities:

- 1) Investment suitability
- 2) Preservation and safety of principal
- 3) Liquidity
- 4) Marketability prior to maturity of each investment
- 5) Diversification
- 6) Yield

For reporting and monitoring purposes and to facilitate investment, the maximum weighted average days to maturity (WAM) for the total portfolio shall be 540 days with a maximum maturity of three (3) years. With these controls in place, the price volatility of the overall portfolio will be minimized and the portfolio will be able to adjust to ongoing market conditions within safe limitations.

Investment guidelines by fund-type are as follows:

1. Pooled Funds

The current operating funds are used for day-to-day operating activities and, accordingly, require short-term liquidity.

Suitability - Any investment eligible in the Investment Policy is suitable for the Pooled Funds.

Safety of Principal - All investments are to be of high quality instruments with no perceived default risk. Market price fluctuations will, however, occur. .

Marketability - Securities with active and efficient secondary markets are necessary in the event of an unanticipated cash requirement. An efficient market is generally defined as having a bid-asked price relationship being no greater than 1/4 of 1 percent of principal value.

Liquidity - Short term investment pools and money market mutual funds shall provide daily liquidity and may be utilized as a competitive yield alternative to fixed maturity investments. . Reserves established in accordance with the City's cash reserves policy or designated for specific purposes and time frames may be invested for longer terms

Diversification - Diversified investment maturities shall provide monthly cash flow based on the anticipated operating needs of the City. Short term investment pools, money market mutual funds and staggered maturities of securities shall provide timely liquidity and may be utilized.

Yield - Attaining a competitive market yield for comparable security-types and portfolio restrictions is the desired objective. The comparative yield of a like-term treasury bill shall be the minimum yield objective.

2. Debt Service Funds

Suitability - Any investment eligible in the Investment Policy is suitable for the Debt Service Funds.

Safety of Principal - All investments are to be of high quality instruments with no perceived default risk. Market price fluctuations will, however, occur. By managing the Debt Service

Fund's portfolio to not exceed the debt service payment schedule, the market risk of the overall portfolio will be minimized.

Marketability - Securities with active and efficient secondary markets are not necessary as the event of an unanticipated cash requirement is not probable.

Liquidity - Short term investment pools and money market mutual funds shall provide daily liquidity and may be utilized as a competitive yield alternative to fixed maturity investments.

Diversification - Short term investment pools, money market mutual funds and staggered maturities of securities shall provide timely liquidity and may be utilized.

Yield - Attaining a competitive market yield for comparable security-types and portfolio restrictions is the desired objective. The comparative yield of a like-term treasury bill shall be the minimum yield objective.

3. Capital Project Funds

Suitability - Any investment eligible in the Investment Policy is suitable for the Capital Improvement Funds.

Safety of Principal - All investments are to be of high quality instruments with no perceived default risk. Market price fluctuations will, however, occur. By managing the Capital Project Fund's portfolio to anticipate the construction and or acquisition cash flow requirements, the market risk of the overall portfolio will be minimized.

Marketability - Securities with active and efficient secondary markets are necessary in the event of an unanticipated cash requirement.

Liquidity - Funds used for construction programs have reasonably predictable draw down schedules. Therefore, investment maturities shall generally follow the anticipated cash flow requirements. Because of the potential for variance from the anticipated draw down schedule and actual expenditures most investment securities shall have active and efficient secondary markets. Investment pools and money market mutual funds are suitable for providing readily available funds.

Diversification - Diversified investment maturities shall provide monthly cash flow based on the anticipated operating needs of the City. Short term investment pools, money market mutual funds and staggered maturities of securities shall provide timely liquidity and may be utilized. Bond proceeds may be invested in a single security or investment if the Investment Officers determine that such an investment is necessary to comply with Federal arbitrage restrictions or to facilitate arbitrage recordkeeping and calculation.

Yield - Attaining a competitive market yield for comparable security-types and portfolio restrictions is the desired objective. The comparative yield of a like-term treasury bill shall be the minimum yield objective.

4. Debt Service Reserve Funds

Suitability - Any investment eligible in the Investment Policy is suitable for the Debt Service Funds. Bond ordinance constraints and insurance company restrictions may create issue-specific considerations in addition to the Investment Policy.

Safety of Principal - All investments are to be of high quality instruments with no perceived default risk. Market price fluctuations will, however, occur. By managing the Debt Service Reserve fund's portfolio to not exceed three years or maturity provisions or, generally, the call provisions of the bond issue, the market risk of the overall portfolio will be minimized.

Marketability - Securities with active and efficient secondary markets are not necessary for Debt Service Reserve funds.

Liquidity - Debt Service Reserve funds have no anticipated expenditures. Therefore, liquidity up to the maturity date or call date is of minor importance.

Diversification - Market conditions and the arbitrage regulations influence the attractiveness of staggering the maturity of fixed rate investments for Debt Service Reserve funds. At no time shall the final debt service payment date of the bond issue be exceeded in an attempt to bolster yield.

Yield - Attaining a competitive market yield for comparable security-types and portfolio restrictions is the desired objective. The comparative yield of a like-term treasury bill shall be the minimum yield objective. Arbitrage regulations should be heeded in investing for yield

Addendum A

CITY OF ROUND ROCK, TEXAS **AUTHORIZED LIST OF BROKER/DEALERS**

1. First Southwest Company
325 North St. Paul Street, Suite 800
Dallas, TX 75201-4652
877-887-3792
2. Frost Capital Markets
100 West Houston Street
San Antonio, TX 78296
800-438-4891
3. Cantor Fitzgerald *
- 14185 Dallas Parkway, Suite 870
Dallas, TX 75254
800-883-6332
4. Piper Jaffray & Co.
111 SW Fifth Street, Ste 1900
Portland, OR 97204-3604
877-664-6133
5. Morgan Stanley
717 Texas Avenue, Ste 3050
Houston, TX 77002
800-324-2708
6. RBC Capital Markets, LLC *
2711 N. Haskell Avenue, Suite 2500
Dallas, TX 75093
866-410-5833
7. Duncan Williams Inc
9801 Westheimer #302
Houston, TX 77042
800-266-5652
8. Merrill Lynch
901 Main Street
Dallas, TX 75202
214-209-2015
9. Wells Fargo Brokerage
1445 Ross Ave
Dallas, TX 75202
214-777-4018
10. Mutual Securities
501 W. Broadway
San Diego, CA 92101
877-664-6133

* Federal Reserve Primary Dealer