

# **CITY OF SAN MARCOS, TEXAS**

## **INVESTMENT POLICY**

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**INVESTMENT POLICY**  
**CITY OF SAN MARCOS**  
**FINANCE DEPARTMENT**

**I. POLICY**

It is the policy of the City of San Marcos to invest public funds in a manner which will optimize interest earnings with maximum security while meeting the daily cash flow demands of the City and conforming to all state and local statutes governing the investment of public funds.

**II. SCOPE**

This Investment Policy (hereafter referred to as Policy) applies to all financial assets of the City. The financial assets covered by this Policy are within funds that are accounted for in the Comprehensive Annual Financial Report and include:

1. General Fund
2. Special Revenue Funds
3. Capital Projects Funds
4. Debt Service Funds
5. Enterprise Funds
6. Internal Service Fund
7. Trust and Agency Funds

and any new funds created by the City unless specifically exempted by the City Council and this Policy. This policy does not apply to funds invested in the City's deferred compensation plan or other retirement plans.

**III. PRUDENCE**

The standard of prudence to be used by investment officers and Finance Administrators shall be the "prudent person" standard and shall be applied in the context of managing an overall portfolio.

*Investments shall be made with judgment 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 probable income to be derived.*

**IV. OBJECTIVES**

All operating and bond funds will be pooled for investment purposes. The primary objectives, in priority order, of the City's investment activities for all funds shall be:

1. Safety: Safety of principal is the foremost objective of the investment program. Investments of the City shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. In order to achieve this objective, diversification is required to minimize credit and market risk and to reduce overall portfolio impact from potential losses on individual securities.
2. Liquidity: The City's investment portfolio will remain sufficiently liquid to enable the City to meet all operating requirements, which might be reasonably anticipated.

3. Public Trust: All participants in the City's investment process shall seek to act responsibly as custodians of the public trust. Investment Officers and employees involved in the investment process shall avoid any transaction that might impair public confidence in the City's ability to govern effectively.
4. Yield: The City's investment portfolio shall be designed with the objective of attaining a market rate of return in accordance with its designated benchmark which is based on the City's cash flow requirements throughout budgetary and economic cycles, commensurate with the City's investment risk constraints and the cash flow characteristics of the portfolio.

## **V. STRATEGY**

The structure and management of the pooled City portfolio will address the varying needs, goals and objectives of each fund. Investment strategies for General Fund, Special Revenue Funds, Capital Projects Funds, Enterprise Funds, and Trust and Agency Funds are designed to assure that anticipated cash flows are matched with adequate liquidity in each fund. A secondary strategy is to create a portfolio structure that will experience minimal volatility during economic cycles. Both may be accomplished by purchasing high quality, short-to-medium term securities that will complement each other in a ladder structure and assure the marketability of those investments should liquidity needs arise.

The Reserve Funds portfolio will address the longer-term nature and needs of the funds. The primary investment strategy will be to utilize financial markets to maximize yield to build the reserves. A secondary objective is to create a portfolio structure that will experience minimal volatility during economic cycles. These objectives may be accomplished by purchasing high credit quality, medium term securities while assuring the marketability of those investments.

Investments for both portfolios are to be chosen in a manner that promotes diversity by market sector, credit and maturity. The maximum dollar weighted average maturity of the portfolios to accomplish investment goals vary based on fund strategy. The maximum allowable maturity for each portfolio also varies to ensure that investment parameters are directly suited to the unique nature of the portfolio.

Investment strategies will address the unique needs for Debt Service Funds to primarily assure investment liquidity adequate to cover the debt service obligation for each consecutive debt service payment. Investments shall progressively fund each succeeding debt service.

Effective cash management is recognized as essential to good fiscal management. Cash management is defined as the process of managing monies in order to ensure maximum cash availability to the City for investment use. The City shall maintain a comprehensive cash management program that 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.

## **VI. DELEGATION OF AUTHORITY**

### **Investment Officers**

Management responsibility for the investment program is hereby delegated to the Director of Finance, the Assistant Director of Finance, the Accounting Manager, and Cash Management Accountant or staff accountant as designated by Director of Finance and they are therefore designated as the Investment Officers under the Act and by resolution of the City Council. The Investment Officer(s) shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

City designated Investment Officers acting in accordance with this standard, written procedures and the Policy and exercising due diligence shall be relieved of personal liability for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments. Investment Advisors / Managers acting under contract to the City are not relieved of personal responsibility.

A contracted non-discretionary Investment Advisor may perform the investment responsibilities under the direction of the Investment Officer(s). The investment management firm selected to transact investment business on behalf of the City will be provided a copy of this Policy to assure that they are familiar with the goals and objectives of the Investment Policy and investment program. All key investment professionals of the investment management firm will be required to return a signed copy of the Certification by Business Organization substantially in the form provided as Appendix B. The investment management firm, which will act in a fiduciary capacity, must be registered with the Securities and Exchange Commission under the Investment Advisor's Act of 1940. The Investment Advisor will be required to manage the City's funds in accordance with the laws of the State of Texas, and Investment Policies and procedures established by the City.

In accordance with the Public Fund Investment Act ( "PFIA" ), Investment Officers shall attend investment training session no less than once every two years receiving not less than 8 hours of instruction relating to investment responsibilities. A newly appointed Investment Officer must attend a training session of at least 10 hours of instruction within twelve months of the date the Officer took office or assumed investment officer duties. The investment training sessions shall be provided by an independent source approved and authorized by the City Council and able to issue PFIA training certification. For purposes of this Policy, an "independent source" from which investment training shall be obtained shall include a professional organization, an institution of higher education or any other sponsor authorized to issue PFIA training certification.

#### Investment Committee

An Investment Committee designated by the City Council consisting of the Finance and Audit committee members, and Accounting Manager is established to review quarterly reports and Policy changes as well as advise the City Council on investment matters. The Investment Committee shall, at least annually or as required by market conditions, review, revise, and adopt a list of authorized broker/dealers that may engage in investment transactions with the City based on the annual review of the financial condition and registrations of dealers and institutions conducted by the Investment Officer(s) (in accordance with this Policy).

## **VII. INVESTMENT PROCEDURES**

The Investment Officer(s) shall establish reasonable commercial written procedures for the operation of the investment program consistent with this Policy. The procedures should include safekeeping, repurchase agreements, wire transfer agreements, banking service contracts and collateral/depository agreements. No person may engage in an investment transaction except as provided under the terms of this Policy and the procedures established by the Investment Officer(s). Investment Committee will make the recommendation when to contract with an Investment Advisor firm depending on market conditions and review / analysis of contract cost versus investment portfolio return.

All investment purchases will be executed using the competitive bidding process and settled on a delivery versus payment (DVP) basis. A minimum of three competitive bids/offers shall be obtained to assure competitive value for the City. The City will practice competitive bidding when purchasing all investments to guarantee the highest rate of return for the desired maturity date.

## **VIII. ETHICS AND CONFLICTS OF INTEREST**

Investment Officers, investment advisers and employees involved in the investment process shall refrain from any personal business relationships with business organizations that could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions. Such employees shall disclose in writing to the City Manager any material financial interests in financial institutions that conduct business with the City, and they shall further disclose any large personal financial/investment positions that could be related to the performance of the City's portfolio. For purposes of this section, an investment officer or employee has a personal business relationship with a business organization if:

1. The Investment Officer or employee owns 10 percent or more of the voting stock or shares of the business organization or owns \$5,000 or more of the fair market value of the business organization.
2. The Investment Officer or employee received funds from the business organization that exceed 10 percent of the Investment Officer's or employee's gross income for the previous year.
3. The Investment Officer or employee has acquired from the business organization during the previous year investments with a book value of \$2,500 or more for the personal account of the Investment Officer or employee.

Investment Officers or employees involved in the investment process with personal business relationships or relatives within the second degree of affinity or consanguinity seeking to sell investments/securities to the City shall disclose the relationship and file a statement with the Texas Ethics Commission and the City Council. Personal business relationships are defined in the PFIA.

## **IX. AUTHORIZED BROKER/DEALERS AND FINANCIAL INSTITUTIONS**

The objective of safety requires that the City transact business with financially strong broker/dealers and financial institutions. Therefore, financial broker/dealers and institutions shall be subject to a screening process by the Investment Officers and/or City contracted Investment Advisor to eliminate those dealers and institutions that lack economic viability or whose past practices put the safety of public capital at risk.

The Investment Advisor under contract will observe the instructions of the City with respect to broker/dealers who are approved to execute transactions involving the City's Managed Funds

These broker/dealers may include "primary" dealers or regional dealers that qualify under Securities and Exchange Commission Rule 15C3-1 (uniform net capital rule). Authorized dealers and institutions shall provide proof of Financial Institutions Regulatory Authority (FINRA) certification, SEC registration, an annual audited financial statement, and a completed broker/dealer questionnaire.

Additional financial institutions may be used for time or demand deposits designed for investment purposes (i.e. not as the primary depository of the City). These institutions may be utilized by the Investment Officer(s) on an ongoing basis to accommodate the need for timely action. Action by the Investment Committee is not required before use of such institutions. Each financial institution will provide policy certification and execute a depository agreement if funds exceed the FDIC insurance limits. The City may utilize third-party rating agencies in order to assess the overall financial strength of potential depositories.

The depository, or its brokerage subsidiary, from which the City obtains banking services including safe-keeping, will not be used for brokerage services in order to perfect ownership on delivery versus payment settlement. The bank may be used for time deposits but these deposits will be bid competitively.

## **X. AUTHORIZED AND SUITABLE INVESTMENTS**

Authorized investments shall be limited to the instruments listed below as authorized and further

described by the PFIA.

1. Obligations of the United States, its agencies and instrumentalities, excluding mortgage-backed securities.
2. Direct obligations of the State of Texas or its agencies and instrumentalities.
3. Other obligations, the principal of and interest of which are unconditionally guaranteed or insured by the full faith and credit of, the State of Texas.
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.
5. Fully insured or collateralized depository certificates of deposit issued by state and national banks in Texas that are:
  - a. Guaranteed or insured by the Federal Deposit Insurance Corporation or its successors; and
  - b. Collateralized to at least 102% in accordance with this Policy (Section XI).
6. Fully collateralized direct repurchase agreements having a defined termination date, collateralized in accordance with this Policy, safe-kept with an independent third party approved by the City, with an executed master repurchase agreement, and placed through a primary government securities dealer, as defined by the Federal Reserve, or a bank doing business in Texas, not to exceed 90 days to the stated maturity.

Flexible repurchase agreements (flex repos) are authorized for investment of bond proceeds, if collateralized in accordance with this Policy, safe-kept with an independent third party approved by the City, with an executed master repurchase agreement, and placed through a primary government securities dealer, as defined by the Federal Reserve. The term of the flex repo may exceed two years but not exceed the anticipated expenditure schedule of the bond proceeds and no party involved with the issuance of the debt shall be involved with the funds reinvestment.

7. Texas local government investment pools as defined and regulated by the PFIA and authorized by the City Council. Investment pools maintaining a \$1.00 net asset value must calculate and report yield to investors in the pool in accordance with federal regulations applicable to money market funds.
8. Commercial paper rated not less than A1/P1 or its equivalent by two nationally recognized rating agencies and not to exceed 270 days to stated final maturity.
9. AAA-rated, SEC registered money market funds as described in Sec. 2256.014 of the PFIA.
10. FDIC insured brokered certificate of deposit securities from banks in any US state, delivered versus payment to the City's safekeeping depository, not to exceed one year to maturity. Before purchase the Investment Officer or adviser must verify the FDIC status of the bank on <https://research2.fdic.gov/bankfind/index.html> to assure that the bank is FDIC insured.
11. Interest bearing or money market accounts in any FDIC insured bank in Texas collateralized as required by this Policy.

## **XI. ALLOWABLE INVESTMENT MATURITY**

1. Financial assets, with the exception of reserve funds, will have a maximum dollar weighted average maturity of twenty-four (24) months, dependent on market conditions, and shall be invested with a stated maturity date not to exceed three years or shorter term .
2. Reserve funds will have a maximum dollar weighted average maturity of twenty-four (24) months, dependent on market conditions, and with a stated maturity not to exceed five years .

## **XII. COLLATERALIZATION**

### **Pledged Collateral**

Collateralization is required on time and demand deposits above FDIC insurance levels. In order to anticipate market changes and provide a level of security for all funds, the collateralization margin level will be maintained at a minimum of 102% of deposits plus accrued interest. The depository counter party shall be made contractually liable for monitoring and maintaining the collateral and required margins daily. Collateral shall be priced at least monthly. The custodian shall provide the required monthly reports directly to the City.

### **Owned Collateral Under a Repurchase Agreement**

Repurchase agreements shall be collateralized to a minimum of 102% of principal and accrued interest. The counter party shall be made contractually liable for monitoring and maintaining the collateral and required margins at all times. Collateral shall be priced daily. The Custodian shall provide the required periodic reports directly to the City.

### **Authorized Collateral**

Collateral shall be limited to the following:

- Obligations of the US Government, its agencies and instrumentalities to include mortgage-backed securities which pass the bank test.
- 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.

For repurchase agreements (Sec. 2256.011), collateral may include cash and obligations of the United States, its agencies or instrumentalities, municipal debt rated A or better and include commercial paper and corporate bonds, when applicable

Pledged collateral shall be held by an independent financial institution approved by the City under a current custodial agreement. Owned collateral shall be held by an independent financial institution approved by the City. Clearly marked evidences of ownership (report or receipt) must be supplied to the City and retained. The right of collateral substitution is granted with prior City approval.

## **XIII. SAFEKEEPING/CUSTODY OF CITY OWNED SECURITIES**

Safekeeping of City owned securities will be provided by the City's banking services depository or its correspondent, or a safekeep agent/custodian. Under a City contract. .

In order to ensure protection for City owned securities, the City requires delivery versus payment procedures for all securities which require book entry delivery.

All security transactions, including collateral for repurchase agreements shall be conducted on a delivery versus payment (DVP) basis to the City's designated safekeeping agent/custodian.



#### **XIV. DIVERSIFICATION**

Diversification of the overall portfolio will be maintained in accordance with the following diversification limits as determined at the time of purchase.

| Security Type                                | Maximum Percent of Portfolio                 |               |
|--|--|---------------|
|  | Financial Assets Except<br>for Reserve Funds | Reserve Funds |
| US Government Treasury Obligations           | 100%   | 100%          |
| US Government Agencies and Instrumentalities | 80%  | 80%           |
| Municipal, County and State Instruments      | 20%  | 20%           |
| Certificates of Deposit                      | 30%  | 30%           |
| Issued by Institution                        | 20%  | 20%           |
| Repurchase Agreements                        | 30%  | 30%           |
| Flex Repurchase Agreements for Bond Proceeds | 100%   | 100%          |
| Local Government Investment Pools            | 100%   | 100%          |
| Ownership of the Investment Pool             | 10%  | 10%           |
| Commercial Paper                             | 40%  | 40%           |
| Limit Per Commercial Paper Issuer            | 10%  | 10%           |
| Money Market Mutual Fund                     | 70%  | 70%           |
| Ownership of the Fund                        | 10%  | 10%           |

#### **XV. INTERNAL CONTROLS**

The Investment Officer(s) shall establish a system of written internal controls that will be reviewed annually with the City or independent auditor of the City along with quarterly investment reports. The controls will be designed to prevent loss of public funds due to fraud, employee error, misrepresentation by third parties, unanticipated market changes, or imprudent actions by employees, contracted investment managers or financial counterparties of the City.

##### **Loss of Rating**

The Investment Officer or investment adviser shall monitor, on no less than a weekly 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 or adviser shall notify the Director of Finance of the loss of rating, conditions affecting the rating and possible loss of principal with liquidation options available, within two weeks after the loss of the required rating.

##### **Monitoring FDIC Status**

The Investment Officer or Investment Adviser shall monitor, on no less than a weekly 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 or Adviser shall immediately liquidate any brokered CD which places the City above the FDIC insurance level.

## **XVI. PERFORMANCE STANDARDS**

The investment portfolio shall be designed with the objective of obtaining a rate of return throughout budgetary and economic cycles, commensurate with the investment risk constraints and cash flow needs of the City. The benchmark the city will utilize is the 24-month trailing average yield of the 2-year Constant Maturity Treasury (CMT). This measure resembles the average maturity of the portfolio and moves in a similar manner to the overall strategy of the portfolio.

## **XVII. REPORTING**

The Investment Officer(s) shall provide the Investment Committee and City Council quarterly investment reports as required by the PFIA. The reports will reflect both detail and summary information enabling the reader to determine the value and risk associated with the portfolio. Market values for the report will be derived from an independent source.

A management report will be included with the quarterly investment report. The management report should include comments on the fixed income markets and economic conditions, diversification by asset class and maturity, allocation restrictions on investments, possible changes in the portfolio structure going forward and thoughts on investment strategies.

## **XVIII. CASH MANAGEMENT PROGRAMS AND ACTIVITIES**

The Department of Finance is committed to the overall success of the City's cash management programs. These programs address a variety of cash management issues, including:

1. The design and implementation of reliable and effective macro cash flow forecasting methodologies to assist Finance Department personnel and Investment Officer(s) in the determination of the amounts of cash available for investment, the time period for which the funds may be invested with a reasonable level of confidence, and a measure of the volatility of specific cash forecasts, which will allow viable determination of the required liquidity.
2. The design and implementation of appropriate "revenue-acceleration programs", aimed at enhancing the speed at which monies are collected and deposited by the City and the elimination of bad debt expense/write-offs.
3. The design and implementation of suitable "controlled disbursement" programs, which will ensure that the City's expenses are met in timely manner, but not in such a way as to jeopardize the earning capacity of the City's portfolio
4. The utilization of modern and efficient techniques and technology for the physical movement of money, taking advantage of technological and operational procedures.
5. The design and implementation of banking relationships which are both favorable to the City and responsive to the day-to-day requirements of the City's complex financial operations.
6. The design of investment policies and procedures to ensure the total safety of all funds while allowing the City to maximize its interest earnings.
7. The design and implementation of appropriate policies and procedures with regard to the safe, proper and effective use of the City's municipal credit authority.

## **XIX. INVESTMENT POLICY ADOPTION**

The City's Investment Policy shall be annually reviewed and adopted by resolution of the City Council. Any modifications made thereto must be noted in the approving Resolution.

## **APPENDIX A**

### **Broker / Dealer Questionnaire & TX PFIA Certification**

## **APPENDIX B**

**PFIA**

**APPENDIX C**  
**CITY OF SAN MARCOS**  
**INVESTMENT PROCEDURES**

**I. PURPOSE**

The purpose of these procedures is to assist Finance Department staff with day-to-day investment operations and assign responsibilities. These procedures are an outline, with individual items to be added or deleted as necessary or appropriate.

**II. CASH REVIEW**

The City Investment Officer(s) must review the cash balances and investment portfolio at least daily, or as needed. Items to be reviewed should include:

- All balances and float amounts at contracted depository bank.
- All pending and maturing investments.
- All incoming wires, bond sales and other anticipated receipts.
- All outgoing wires, bond and coupon payments (debt service) and other anticipated cash disbursements.

**III. INVESTMENT SELECTION**

The City Investment Officer(s) determines how much of the cash balance is available for investment and selects the maximum maturity date to fund upcoming liabilities.

The Investment Officer(s) and/or the contracted Investment Advisor will review market conditions in conjunction with approved brokers to search for suitable investments on at least a weekly basis.

Information including the following is used to determine optimal maturity to take advantage of current and expected interest rate environments:

- Market information (yield analysis, spread analysis, and future expectations)
- General trends of economic statistics.

Input from independent data services (Bloomberg, Reuters, etc.)

**IV. PURCHASING AND INVESTMENT**

The Policy requires establishment and approval of an authorized broker/dealer list with whom the City may transact business. The broker/dealer questionnaire helps provide the following evaluation:

- Financial condition, strength and capability to fulfill commitments.
- Overall reputation with other broker/dealers and investors.

- Service history
- FINRA status of the broker/dealer.
- Background and expertise of the individual representative.

The City investment officer(s) and/or the contracted Investment Adviser / Manager will contact a minimum of three or appropriate number of broker/dealers for bids/offers based on market evaluation, Investment Policy and collateral limitations, and cash flow needs.

The following will be determined with the broker/dealer:

- Settlement basis – i.e. cash (same day), regular (next day), or when-issued (issue date) if a new agency issue.
- Amount available for investment,
- Type of security to be purchased or excluded.
- Targeted stated maturity, or maturity range.

If the City is working with an investment advisor, the advisor will perform screenings of broker-dealers to ensure they meet internal metrics to be an approved firm. Final approval will be made by the City.

Any investment pool requires a Council resolution. Authorized individuals (PIN) resolutions and delivery instructions must be in place prior any transactions with the pool. All pool transactions are initiated and controlled by City Investment Officer(s).

All investment purchases will be executed using the prescribed competitive bidding process. A minimum of three competitive offers will be obtained All investment purchases will be executed in compliance with the Internal Revenue Service's Fair Market Rules.

Before concluding the transaction, the City investment officer(s) and/or the Investment Adviser must verify the following:

- The security meets all cash flow and Policy criteria.
- The security structure including any imbedded options such as call provisions or coupon adjustments is noted.
- Yield calculations and settlement amounts are accurate.
- Total purchase cost (including accrued interest) are reported to the custodian.

And,

- Advises the successful provider that their offering has been selected for purchase.
- Notifies any unsuccessful broker/dealers. Best price may be disclosed.

Prior to any transaction settlement date, the City Investment Officer and/or Investment Adviser and broker/dealer shall exchange and review the following settlement instructions to ensure prompt, and uninterrupted settlement.

- Delivery instructions for the third-party safekeeping agent.

- 
- Breakdown and total transaction amount.
- Settlement date.
- CUSIP number of security.
- 
- 

## **V. SETTLEMENT AND FOLLOW-THROUGH**

The City Investment Officer and/or the Investment Adviser will obtain a written or electronic record for the City's records

City follow-up procedures may include:

- Internal provision of receipt or disbursement of funds.
- Internal transfer or wiring of funds.
- Validation of written "safekeeping receipt".
- Immediate notification by the adviser if a fail has occurred.