



INVESTMENT POLICY

POLICY

It is the policy of the City of Canyon (the "City") that after allowing for the anticipated cash flow requirements of the City and giving due consideration to the safety and risk of investment, all available funds shall be invested in conformance with these legal and administrative guidelines, seeking to optimize interest earnings to the maximum extent possible.

Effective cash management is recognized as essential to good fiscal management. Investment interest is a source of revenue to the City. The City's investment portfolio shall be designed and managed in a manner designed to maximize this revenue source, to be responsive to public trust, and to be in compliance with legal requirements and limitations.

Investments shall be made with the primary objectives of:

- * **Safety** and preservation of principal
- * Maintenance of sufficient **liquidity** to meet operating needs
- * **Public trust** from prudent investment activities
- * Optimization of **interest earnings** on the portfolio

PURPOSE

The purpose of this investment policy is to comply with Chapter 2256 of the Government Code ("Public Funds Investment Act"), which requires the City to adopt a written investment policy regarding the investment of its funds and funds under its control. The Investment Policy addresses the methods, procedures and practices that must be exercised to ensure effective and judicious fiscal management of the City's funds.

SCOPE

This Investment Policy shall govern the investment of all financial assets of the City. These funds are accounted for in the City's Comprehensive Annual Financial Report (CAFR) and include:

- General Fund
- Water Works & Sewer System Fund
- Golf Course Fund
- C.E.D.C. Funds
- W/S Bond Funds
- Emergency Management Fund
- Library Gift and Memorial Fund
- Board of City Development Fund
- LEOSE Fund
- D-Fi-It Program
- Employee Flower Fund
- Vol. Firemen's Funds

- All subsidiary funds and any new fund created unless specifically exempted

The City may consolidate cash balances from all funds to manage bank service needs and enhance investment earnings. Investment income will be allocated to the various funds based on their respective participation and in accordance with generally accepted accounting principles.

This Investment Policy shall apply to all transactions involving the financial assets and related activity for all the foregoing funds.

INVESTMENT OBJECTIVES

The City shall manage and invest its cash with four primary objectives, listed in order of priority: **safety, liquidity, public trust, and yield, expressed as optimization of interest earnings.** The safety of the principal invested always remains the primary objective. All investments shall be designed and managed in a manner responsive to the public trust and consistent with state and local law.

The City shall maintain a comprehensive cash management program, which includes collection of account receivables, vendor payments in accordance with invoice terms, and prudent investment of available cash. Cash management is defined as the process of managing monies in order to insure adequate cash availability and optimum earnings on short-term investment of idle cash.

Safety [PFIA 2256.005(b)(2)]

Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit and interest rate risk.

- Credit Risk – The City will minimize credit risk, the risk of loss due to the failure of the issuer or backer of the investment, by:
 - Limiting investments to the safest types of investments
 - Pre-qualifying the financial institutions and broker/dealers with which the City will do business
 - Diversifying issuer credit risk, when appropriate, so that potential losses on individual issuers will be minimized.
- Interest Rate Risk – the City will minimize the risk that the interest earnings and the market value of investments in the portfolio will fall due to changes in general interest rates, by:
 - Structuring the investment portfolio so that investments mature to meet cash requirements for ongoing operations, thereby avoiding the need to liquidate investments prior to maturity.
 - Investing operating funds primarily in certificates of deposit, shorter-term securities, money market mutual funds, or local government investment pools functioning as money market mutual funds.
 - Diversifying maturities and staggering purchase dates to minimize the impact of market movements over time.
 - Utilizing any other method of investment management allowable by the Public Funds Investment Act deemed most advantageous based on current market conditions.

Liquidity [PFIA 2256.005(b)(2)]

The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by structuring the portfolio so that investments mature concurrent with cash needs to meet anticipated demands.

Public Trust

All participants in the City's investment process shall seek to act responsibly as custodians of the public trust. Investment officers shall avoid any transaction that might impair public confidence in the City's ability to govern effectively.

Yield (Optimization of Interest Earnings) [PFIA 2256.005(b)(3)]

The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Return on investment is of secondary importance compared to the safety and liquidity objectives described above.

RESPONSIBILITY AND CONTROL

Delegation of Authority [PFIA 2256.005(f)]

The City Commission designates the City Manager as the Chief Financial Officer, and he/she and the Director of Finance as the City's Investment Officers. An Investment Officer is authorized to execute investment transactions on behalf of the City. No person may engage in an investment transaction or the management of City funds except as provided under the terms of this Investment Policy as approved by the City Commission. The investment authority granted to the Investment Officers is effective until rescinded by the City Commission.

Quality and Capability of Investment Management [PFIA 2256.005(b)(3)]

The City shall provide periodic training in investments for the designated Investment Officers and other investment personnel through courses and seminars offered by professional organizations, associations, and other independent sources in order to insure the quality and capability of investment management in compliance with the Public Funds Investment Act.

Training Requirement (PFIA 2256.008)

In accordance with the Public Funds Investment Act, Investment Officers shall attend investment training no less often than once every two years, aligned with the City's fiscal year end, and shall accumulate not less than 8 hours of instruction relating to investment responsibilities. A newly appointed Investment Officer must attend training accumulating at least 10 hours of instruction within twelve months of the date the officer took office or assumed the officer's duties. Approved training sources include:

- Government Finance Officers Association
- Government Finance Officers Association of Texas
- Government Treasurers' Organization of Texas
- Texas Municipal League
- University of North Texas

Internal Controls (Best Practice)

The Chief Financial Officer is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the City are protected from loss, theft, or misuse. The internal control structure shall be designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived; and (2) the valuation of costs and benefits requires estimates and judgments by management.

Accordingly, the Chief Financial Officer shall establish a process for annual independent review by the external auditor to assure compliance with policies and procedures. The internal controls shall address the following points.

- Control of collusion.
- Separation of transactions authority from accounting and record keeping.
- Custodial safekeeping.
- Clear delegation of authority to subordinate staff members.
- Written confirmation for telephone (voice) transactions for investments and wire transfers, and
- Development of a wire transfer agreement with the depository bank or third-party custodian

Prudence (PFIA 2256.006)

The standard of prudence to be applied by the Investment Officer shall be the “prudent investor rule.” This rule states that “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.”

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

- The investment of all funds, or funds under the City’s control, over which the officer had responsibility rather than a consideration as to the prudence of a single investment.
- Whether the investment decision was consistent with the written approved investment policy of the City.

Indemnification (Best Practice)

The Investment Officer, acting in accordance with written procedures and exercising due diligence, shall not be held personally responsible for a specific investment’s credit risk or market price changes, provided that these deviations are reported immediately and the appropriate action is taken to control adverse developments.

Ethics and Conflicts of Interest [PFIA 2256.005(i)]

Investment Officers and employees involved in the investment process shall refrain from personal business activity that would conflict with the proper execution and management of the investment program, or that would impair their ability to make impartial decisions. Employees and Investment Officers shall disclose any material interests in financial institutions with which they conduct business. They shall further disclose any personal financial/investment positions that could be related to the performance of the investment portfolio. Employees and Investment Officers shall refrain from undertaking personal investment transactions with the same individual with which business is conducted on behalf of the City.

An Investment Officer of the City who has a personal business relationship with an organization seeking to sell an investment to the City shall file a statement disclosing that personal business interest. An Investment Officer who is related within the second degree by affinity or consanguinity to an individual seeking to sell an investment to the City shall file a statement disclosing that relationship. A statement required under this subsection must be filed with the Texas Ethics Commission and the City Commission.

SUITABLE AND AUTHORIZED INVESTMENTS

Portfolio Management

The City currently has a “buy and hold” portfolio strategy. Maturity dates are matched with cash flow requirements and investments are purchased with the intent to be held until maturity. However, investments may be liquidated prior to maturity for the following reasons:

- An investment with declining credit may be liquidated early to minimize loss of principal.
- Cash flow needs of the City require that the investment be liquidated.

Investments [PFIA 2256.005(b)(4)(A)]

City funds governed by this Policy may be invested in the instruments described below, all of which are authorized by the Public Funds Investment Act. Investment of City funds in any instrument or security not authorized for investment prohibited. The City will not be required to liquidate an investment that becomes unauthorized subsequent to its purchase.

I. Authorized

1. Obligations of, or guaranteed by governmental entities including:
 - a) Obligations, including letters of credit, of the United States or its agencies and instrumentalities, including the Federal Home Loan Bank;
 - b) Direct obligations of the State of Texas or its agencies and instrumentalities;
 - c) Other obligations, the principal of and interest on 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, including obligations that are fully guaranteed or insured by the Federal Deposit Insurance Corporation or by the explicit full faith and credit of the United States;
 - d) Obligations of states, agencies, counties, cities, and other political subdivisions of any state having been rated as to investment quality by a nationally recognized investment rating firm and having received a rating of not less than A or its equivalent; and
 - e) Interest-bearing banking deposits that are guaranteed or insured by:
 - 1) The Federal Deposit Insurance Corporation or its successor; or
 - 2) The National Credit Union Share Insurance Fund or its successor.
2. Certificates of Deposit, issued by a depository institution that has its main office or a branch office in this state:
 - a) And such certificates of deposits are:
 - 1) Guaranteed or insured by the Federal Deposit Insurance Corporation, or its successor; or the National Credit Union Share Insurance Fund, or its successor;
 - 2) Secured by obligations that are described by the PFIA, which are intended to include all direct federal agency or instrumentality issued mortgage backed securities that have a market value of not less than 102% of the principal amount of the certificates or in any other manner and amount provided by law for deposits of the investing entities;
 - 3) Secured in accordance with Chapter 2257 or in any other manner and amount provided by law for deposits of the City.

- b) Certificates of Deposit made with the following conditions:
- 1) The funds are invested by an investing entity through
 - a. A broker that has its main office or a branch office in the state of Texas and is selected from a list adopted by the City as required by Section 2256.025; or
 - b. The broker or the depository institution selected by the City under Subdivision a) arranges for the deposit of the funds in certificates of deposit in one or more federally insured depository institutions, wherever located, for the account of the City;
 - c. The full amount of the principal and accrued interest of each of the certificates of deposit is insured by the United States or an instrumentality of the United States;
 - d. The City appoints the depository institution selected depository institution under Subdivision a), or a clearing broker-dealer registered with the Securities and Exchange Commission and operating pursuant to Securities and Exchange Commission Rule 15c3-3 as custodian for the City with respect to the certificates of deposit issued for the account of the City.
 3. Money Market Mutual Funds that are 1) registered and regulated by the Securities and Exchange Commission, 2) managed in compliance with money market fund regulations, 3) rated AAA by at least one nationally recognized rating service, and 4) seek to maintain a stable net asset value of \$1.0000 per share.
 4. Local government investment pools, which 1) meet the requirements of Chapter 2256.016 of the Public Funds Investment Act, 2) are rated no lower than AAA or an equivalent rating by at least one nationally recognized rating service, 3) *seek to maintain a \$1.00 net asset value*, and 4) are authorized by resolution or ordinance by the City Commission.
 5. Certificates of Deposit and Money Market Accounts through cooperative programs such as CDARS (Certificates of Deposit Account Registry Service) and ICS (Insured Cash Sweep) which spread deposits to provide \$250,000 FDIC Insurance Coverage per Financial Institution and insure the total deposit.
 6. 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.

It is the policy of the City to provide a competitive environment for all individual investment purchases and sales, and financial institution, money market mutual fund, and local government investment pool selections.

All security transactions shall be executed using the delivery versus payment method. That is, funds shall not be wired or paid until verification has made that the correct security was received by the City's safekeeping agent. The City shall contract with a bank or banks for the safekeeping of securities owned by the City as part of its investment portfolio. Securities owned by the City shall be held in the City's account as evidenced by safekeeping receipts of the institution holding the securities. Safekeeping institutions shall be independent from the parties involved in the investment transaction.

All prudent measures will be taken to liquidate an investment that is downgraded to less than the required minimum rating. (*PFIA 2256.021*)

II. **Not Authorized [PFIA 2256.009(b)(1-4)]**

The City's authorized investments are more restrictive than those allowed by State law. Not all investments authorized by State Law are authorized by this Policy. The City prohibits investments in all collateralized mortgage obligations. State law specifically prohibits investment in the following investment securities:

1. Obligations whose payment represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pay no principal;
2. Obligations whose payment represents the principal stream of cash flow from the underlying mortgage-backed security collateral and bears no interest;
3. Collateralized mortgage obligations that have a stated final maturity date of greater than 10 years.

The City is not required to liquidate investments that were authorized investments at the time of purchase. The City will take prudent measures to liquidate any investment that loses its required minimum rating.

INVESTMENT PARAMETERS

Maximum Maturities [PFIA 2256.005(b)(4)(B)]

The longer the maturity of investments, the greater their price volatility. Therefore, it is the City's policy to concentrate its investment portfolio in shorter-term investments in order to limit principal risk caused by changes in interest rates.

The City attempts to match its investments with anticipated cash flow requirements. The City will not directly invest in investments maturing more than three (3) years from the date of purchase; however, the above described obligations, certificates, or agreements may be collateralized using longer dated investments.

Diversification [PFIA 2256.005(b)(3)]

The City recognizes that investment risks can result from issuer defaults, market price changes or various technical complications leading to temporary illiquidity. Risk is controlled through portfolio diversification that shall be achieved by the following general guidelines:

- Limiting investments to avoid overconcentration in a specific issuer or business sector (excluding those deposit that are fully insured and collateralized in accordance with state and federal law),
- Restricting/prohibiting investments that have higher credit risks (example: commercial paper),
- Investing in varying maturities, and
- Continuously investing a portion of the portfolio in cash equivalent options such as local government investment pools (LGIPs), money market funds, or interest-bearing demand or money market depository accounts to ensure that appropriate liquidity is maintained in order to meet ongoing obligations.

Investment Policy Certification

All local government investment pools and discretionary investment management firms must sign a certification acknowledging that the organization has received and reviewed the City's Investment Policy, and that reasonable procedures and controls have been implemented to preclude investment transactions that are not authorized by the City's Policy in accordance with the PFIA.

Authorized Broker/Dealers

The City shall, at least annually, review, revise, and adopt a list of qualified broker/dealers authorized to engage in securities transactions with the City. Authorized firms include primary dealers or secondary dealers that qualify

under Securities & Exchange Commission Rule 15C3-1 (Uniform Net Capital Rule). The Authorized Broker/Dealer list is attached in Appendix A.

Depositories

The City will select and designate a qualified primary bank depository in compliance with State law and the City's purchasing policy. Additionally, the City may utilize other depository institutions to expand deposit placement opportunities or provide specialty services.

All depository balances shall be insured or collateralized in compliance with applicable State law. The City reserves the right, in its sole discretion, to accept or reject any form of insurance or collateralization pledged towards depository deposits. Depositories will be required to sign an Agreement with the City. The Agreement shall address any concerns in relation to acceptable collateral, levels of collateral, substitution and addition of collateral, and reporting and monitoring of collateral. The collateralized deposit 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:

- The Agreement must be in writing;
- The Agreement has to be executed by the Depository and the City contemporaneously with the acquisition of the asset;
- The Agreement must be approved by the Board of Directors or Designated Committee of the Depository and a copy of the meeting minutes must be delivered to the City; and
- The Agreement must be part of the Depository's "official record" continuously since its execution.

Collateral will be held by a third-party custodian designated by the City and pledged to the City as evidenced by pledge receipts of the institution with which the collateral is deposited. Original pledge receipts shall be obtained. Collateral may be held by a Federal Reserve Bank or branch of a Federal Reserve Bank, a Federal Home Loan Bank, or a third party bank approved by the City and eligible under State law.

REPORTING (PFIA 2256.023)

Methods

The Investment Officers shall prepare an investment report on a quarterly basis that summarizes investment strategies employed in the most recent quarter and describes the portfolio in terms of investments and maturities, and shall explain the total investment return for the quarter.

The quarterly investment report shall include a summary statement that will allow the City to ascertain whether investment activities during the reporting period have conformed to the Investment Policy. The report will be provided to the City Commission. The report will include the following:

- A listing of individual investments held at the end of the reporting period.
- Unrealized gains or losses resulting from appreciation or depreciation by listing the beginning and ending book and market value of investments for the period.
- Additions and changes to the market value during the period.
- Average weighted yield to maturity of portfolio as compared to applicable benchmark.
- Listing of investments by maturity date.
- Fully accrued interest for the reporting period.
- The percentage of the total portfolio that each type of investment represents.

- Statement of compliance of the City’s investment portfolio with state law and the investment strategy and policy approved by the City Commission.
- Signatures of each Investment Officer.

The market value of the portfolio will be calculated, and investment credit ratings will be confirmed on a quarterly basis in compliance with the reporting requirements. In determining market value and credit ratings, sources independent of the investment provider will be pursued.

“Weighted average yield to maturity” shall be the standard on which investment performance is calculated.

As a function of the annual audit, the quarterly investment reports shall be reviewed by the external auditor and the results of that review provided to the City Commission.

INVESTMENT STRATEGIES

Operating Funds Strategy

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

Safety of Principal - All investments shall be of high quality with no perceived default risk. Market price fluctuations may occur. However, by managing the weighted average days to maturity for the Operating Fund’s portfolio to less than 270 days and restricting the maximum allowable maturity to two years, the price volatility of the overall portfolio will be minimized.

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

Liquidity - The Operating Funds requires the greatest short-term liquidity of any of the Fund types. Cash equivalent investments will provide daily liquidity and may be utilized as a competitive yield alternative to fixed maturity investments.

Diversification - Investment maturities should be staggered throughout the budget cycle to provide cash flow based on the anticipated operating needs of the City. Market cycle risk will be reduced by diversifying the appropriate maturity structure out through two years.

Yield - Attaining a competitive market yield for comparable investment-types and portfolio restrictions is the desired objective. The yield of an equally weighted, rolling three-month Treasury Bill portfolio will be the minimum yield objective.

Construction and Capital Improvement Funds Strategy

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

Safety of Principal – All investments will be of high quality with no perceived default risk. Market fluctuations may occur. However, by restricting the maximum maturity to the lesser of the anticipated cash flow requirements, three years or the IRS defined temporary period, the market risk of the portfolio will be minimized.

Marketability - The balancing of short-term and long-term cash flow needs requires the Construction and Capital Improvement Funds portfolio to have securities with active and efficient secondary markets.

Liquidity - Construction and Capital Improvement Funds used as part of a CIP plan or scheduled repair and replacement program are reasonably predictable. However, unanticipated needs or emergencies may arise. Maintaining minimum cash equivalent investment amounts will reduce the liquidity risk of unanticipated expenditures.

Diversification - Investment maturities should blend the short-term and long-term cash flow needs to provide adequate liquidity, yield enhancement and stability. A “barbell” maturity ladder may be appropriate.

Yield - Attaining a competitive market yield for comparable investment-types and portfolio structures is the desired objective. The yield of an equally weighted, rolling six-month Treasury Bill portfolio will be the minimum yield objective.

Debt Service Funds Strategy

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

Safety of Principal - All investments shall be of high quality with no perceived default risk. Market price fluctuations may occur. However, by managing Debt Service Funds 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 flow requirement is not probable.

Liquidity - Debt Service Funds have predictable payment schedules. Therefore, investment maturities should not exceed the anticipated cash flow requirements. Cash equivalent investments may provide a competitive yield alternative for short term fixed maturity investments.

Diversification - Market conditions influence the attractiveness of fully extending maturity to the next “unfunded” payment date. Generally, if investment rates are anticipated to decrease over time, the City is best served by locking in most investments. If the interest rates are potentially rising, then investing in shorter and larger amounts may provide advantage. At no time shall the debt service schedule be exceeded in an attempt to bolster yield.

Yield - Attaining a competitive market yield for comparable investment-types and portfolio restrictions is the desired objective. The yield of an equally weighted, rolling three-month Treasury Bill portfolio shall be the minimum yield objective.

INVESTMENT POLICY ADOPTION [PFIA 2256.005(e)]

The City’s investment policy shall be adopted by resolution of the City Commission. It is the City’s intent to comply with state laws and regulations. The City’s investment policy shall be subject to revisions consistent with changing laws, regulations, and needs of the City. The City Commission shall adopt a resolution stating that it has reviewed the policy and investment strategies annually, approving any changes or modifications.

Appendix A.
Authorized Broker/Dealer List

At this time, the City solely uses Happy State Bank for all investments. No authorized broker/dealer listed are required at this time.