

# Financial and Budgetary Policies

(Revised June, 2019)

## I. Introduction

The City of Pecos, Texas maintains comprehensive financial policies covering a broad range of the elements of the City's financial plans and financial systems that underlay the management of overall City resources. These policies are intended to:

1. Link long-term financial planning with short-term daily operations and decision-making;
2. Maintain and improve the City's financial position;
3. Maintain and improve the City's credit ratings by meeting or exceeding the requirements of rating agencies through sound financial policies;
4. Maintain and increase investor confidence in the City and to provide credibility to the citizens of the City regarding financial operations; and
5. Effectively conduct asset-liability management of the City's balance sheet.

## II. Operating Budget

1. The City's Annual Budget Ordinance will be balanced each year and will be adopted by fund and department 30 days prior to the beginning of the subject fiscal year.
2. In order to force a higher level of planning throughout all levels of City government, the annual budget process will focus on future needs through a Capital Improvements Plan and Financial Forecast, as discussed later in this document.
3. The annual budget process will consist of a series of public meetings where Council and staff discuss needs in relation to the City's mission statement and Council's adopted priorities.

## III. Revenue Policy

1. Ad Valorem Tax –Estimated revenue from the Ad Valorem Tax levy will be budgeted as follows:
  - a.) Assessed valuation will be provided by the Reeves County Tax Assessor.
  - b.) The property tax rate will be set each year based upon the costs of providing general governmental services, meeting debt service obligations and building or maintaining any reserves or fund balances the Council deems necessary.
2. State revenues fluctuate according to the general economic condition of the state and the county. Accordingly, the City will budget these revenues in a conservative manner using guidance from

recognized State agencies or financial publications to determine predicted rates of growth in these revenues.

3. User Fees – The City Council (the “Council”) will set user fees annually by listing such fees within a fee schedule adopted with the Annual Budget Ordinance. In the case of the water and sewer enterprises, the Council will continue to use a professionally designed rate model in order to determine the most appropriate rates based upon current and future expenses. User fees will maximize charges for services that can be individually identified and where costs are directly related to the provision of or to the level of service provided.

Emphasis of user fees results in the following benefits:

- 1.) The burden on the Ad Valorem tax is reduced.
- 2.) User fees are paid by all users, including those exempt from property taxes.
- 3.) User fees help minimize subsidization in any instance where there are requirements in order to qualify for the use of the service and the service is not provided to the general public.
- 4.) User fees produce information on the demand level for services and help to make a connection between the amount paid and the services received.

4. Interest Income – Interest income is subject to variability based upon changes in prevailing interest rates, which cannot be predicted with certainty. Such revenue shall therefore be budgeted in a conservative manner within the Annual Budget Ordinance and shall comply with the Asset – Liability Management section of this policy.

5. Grant Funding – Staff will pursue opportunities for grant funding. Application for grant funding will be made after a grant has been evaluated for consistency with the Council’s goals and compatibility with City programs and objectives. Staff must have Council approval to apply for a grant for any amount over \$50,000 and for any grant that requires a local dollar match. All awarded grants can only be accepted by Council action at which time the related budget shall be established.

- a.) Grants that have been awarded in prior years and are recurring in nature will be included and addressed through the annual budget process.
- b.) For grants that fund operating expenditures but have a funding termination date, the transition or termination plan including any other funds intended to support future services, must be presented to the Council prior to acceptance.
- c.) The grant manager for each grant shall be assigned by the City Manager. The grant manager is responsible for all grant monitoring, compliance and reporting. The grant manager will provide copies of all documents to the Finance Director. The Finance Director will maintain a grant file by fiscal year for each active grant.
- d.) For grants involving federal funds, the grant manager is responsible for checking the list of federally debarred contractors prior to awarding any contracts.

6. Budgetary Responsibilities – The City Manager shall develop initial budget estimates of applicable revenues. Those estimates are to be supported by variables (base, rate, etc.) that comprise such revenue. Monitoring of the revenue budget shall be performed by the Finance Director in a timely manner throughout the fiscal year and shall include an analysis of actual versus budgeted variances. Compliance of revenue with all laws and/or regulations is primarily the responsibility of the revenue-initiating department.

#### Revenue Spending Policy

1. The City will follow a revenue spending policy that provides guidance for programs with multiple revenue sources. The Finance Department, as directed by the Finance Director, will use resources in the following hierarchy as appropriate: bond proceeds, federal funds, State funds, City funds.
2. For purposes of fund balance classification, expenditures are to be spent from restricted fund balance first, followed in order by committed fund balance, assigned fund balance, and lastly, unassigned fund balance. The Finance Director has the authority to deviate from this policy if it is in the best interest of the City, however the Council will be notified within the next two City Council meetings.

#### Characteristics of the Revenue System

The City strives for the following optimum characteristics in its revenue system:

1. Simplicity and Certainty. The City shall strive to keep the revenue classification system simple to promote understanding of the revenue sources. The City shall describe its revenue sources and enact consistent collection policies to provide assurances that the revenue is collected according to budgets and plans.
2. Equity. The City shall make every effort to maintain equity in its revenue system structure. The City shall minimize all forms of subsidization between entities, funds, services, utilities, and customers.
3. Centralized Reporting. Receipts will be submitted daily to the Finance Department for deposit and investment. Daily transaction reports and supporting documentation will be prepared.
4. Review of Fees and Charges. The City shall review all fees and charges annually in order to match fees and charges with the cost of providing that service, except in cases where the social benefit impact outweighs the objective of full cost recovery (e.g. recreational programs, etc.)
5. Aggressive Collection Policy. The City shall follow an aggressive policy of collecting revenues. Utility services will be discontinued (i.e. turned off) for non-payment in accordance with established policies and ordinances. The Finance Director may place a delinquent account on a re-payment plan prior to turning the account over for collection. Other receivables that are 120 days or greater shall be sent to collections. The Finance Director is authorized to “write-off” all non-collectible accounts and specify said action in the annual audit.

#### Non-Recurring Revenues

- 1.) One-time or non-recurring revenues will not be used to finance current ongoing operations.
- 2.) Non-recurring revenues will be used only for one-time expenditures such as capital needs.

### Utility Rates

The City shall review and adopt utility rates annually that generate revenues required to cover operating expenditures, meet the legal restrictions of all applicable bond covenants, and provide for an adequate level of working capital. This policy does not preclude drawing down cash balances to pay for debt service obligations, to retire bonded indebtedness or to undertake capital projects.

### Interest Income

Interest earned from investment of available monies, whether pooled or not, shall be distributed to the funds in accordance with the equity balance of the fund from which monies were invested.

### User-Based Fees and Service Charges

With respect to utility user charges, and impact fees associated with development, the direct and indirect costs of that service shall be offset wholly by a fee. There shall be an annual review of fees and charges to ensure that the fees provide adequate coverage of costs of services. Full fee support shall be obtained from development application processing and related development services.

Enterprise utilities and capital improvements for utilities shall be wholly offset by fees. However, from time to time, the Finance Director may establish programs or certain procedures to place a delinquent account on a repayment program for delinquent utility charges. With respect to Special Revenue Funds and other City provided services (i.e. recreation programs), fees should partially offset services as deemed appropriate by the City Council. All fees recorded will be direct charges to a specific person or entity using the service; requests for third party charges will not be accepted.

### Intergovernmental Revenues/Grants

Grant revenues shall be spent for the purpose(s) intended. The City shall review grant match requirements and not rely on grants for the basic operating budget nor rely on one-time revenue sources.

### Revenue Monitoring

Revenues actually received are to be regularly compared to the budgeted revenues and reported to the City Council at least quarterly.

### Revenue Projections

The City shall project current year revenues based on the previous five year history and will update this projection annually. Each existing and potential revenue source shall be re-examined annually.

Operating Revenues will be projected out three to five years for report at mid-year. Exception: In the event significant delta conditions, such as ( new re-occurring land use or development) will dramatically skew the projection history, then the Finance Director is authorized to adjust the five year history "current year" revenue number to better reflect changed conditions.

## **IV. Expenditure Policy**

1. Expenditure budgets shall be monitored throughout the fiscal year by department heads, the Finance Director and the City Manager. Budget compliance, which includes electronic obligations, is the responsibility of the department heads and the City Manager.

2. Budgeted funds will only be spent for categorical purposes for which they are intended. Budget amendments may be made to reflect unexpected expenses and must be approved by vote of the

Council. Appropriations of debt proceeds will be made only for the purpose for which such debt instrument was issued or for the payment of debt principal and interest.

3. Budgeted expenditures for debt service for any variable rate debt or synthetic variable rate debt will be set to at least the average of the prior five years.

4. For continuing contracts, funds will be appropriated in the annual budget ordinance to meet current year obligations arising under the contract.

5. Payroll will be processed in accordance with the requirements of the Fair Labor Standards Act and other applicable federal and state laws. Benefit payments will be made in accordance with the City's Personnel Policy and applicable laws.

6. The City may utilize non-capital operating leases or installment purchase loans for the procurement of copiers, multifunction copiers/printer type machines and for personal computers.

7. The City will fund current expenditures with current resources and will strive to avoid balancing budgets utilizing one-time revenues.

8. The City will employ the use of the carryover method for reappropriation of outstanding purchase orders and contracts for multiple year projects and purchases as of the end of each fiscal year into the new fiscal year. The process shall be explained in each year's budget process.

#### **V. Reserve/Fund Balance Policy**

1. Appropriated fund balance in any fund will not exceed the sum of cash and investments less the sum of liabilities, encumbrances, and deferred revenues arising from cash receipts as those figures stand at the close of the fiscal year next proceeding the budget year.

2. The City will strive to maintain a General Fund unassigned fund balance of 25% of annual expenses plus debt payment coverage. Unassigned fund balance is defined as the portion of fund balance that remains available for appropriation by the City Council after all commitments for future expenditures, required reserves defined by State statutes, and Council-established assignments have been calculated. The percentage is to be determined by dividing the unassigned fund balance amount by actual expenditures of the then completed fiscal year.

a.) Purpose of Reserve: These funds will be utilized to avoid cash flow interruptions, generate interest income, eliminate the need for short-term borrowing, and maintain the City's credit ratings.

b.) Reserve Drawdown: The available fund balance may be purposefully drawn down below the target percentage for emergencies, economic influences, nonrecurring expenditures, or major capital projects.

c.) Reserve Replenishment: If the available fund balance falls below the target percentage for two consecutive fiscal years, the City will replenish funds by direct appropriation in the next budget developed for the fiscal year after the occurrence is known. In that instance, the City will annually appropriate at least 25% of the difference between the target percentage level and the actual

balance until the target level is met. In the event appropriating 25% is not feasible, the City will appropriate a lesser amount and shall reaffirm by Council resolution its commitment to fully replenish the fund balance over a longer designated period of time.

d.) Any General Fund unassigned fund balance that exceeds the target goal range may be used to reduce general fund debt or fund major capital projects.

3. The City will appropriate within the annual budget a contingency appropriation each fiscal year. The minimum level of contingency is 1% of budgeted general fund expenditures and the maximum is an amount equal to the revenue generated by a \$.01 ad valorem tax rate plus the approved provision for personnel merit bonuses.

4. The City's goal will be to maintain a minimum cash balance in both the water and sewer operating funds (separately) of 25% of actual expenditures of the most recent completed fiscal year, plus debt payment coverage. These funds will be utilized to avoid cash flow interruptions, generate interest income, fund capital expenditures, eliminate the need for short-term borrowing, and maintain the City's credit ratings.

## **VI. Asset-Liability Management**

1. The City will seek to incorporate coordinated investment and debt structuring decisions with the goal to mitigate, or hedge, cash flow risks while maximizing opportunities to complete needed infrastructure projects.

2. The City considers short-term investments to be effective hedges to variable rate debt because movements in interest rates should have offsetting impacts upon both.

a.) Given the prevalent patterns of business, economic and interest rate cycles, the City may strive to match temporary increases in interest income to temporary increases in interest expense through the use of variable rate debt or synthetic variable rate debt.

b.) This recognizes that variable rate debt generally offers lower interest costs and that the use of higher interest income to offset higher interest expense is preferable to creating a budget imbalance due to reliance upon temporarily increased interest income.

3. The Finance Director is designated to monitor and report on financial market conditions and their impact on performance of debt, investments, and any interest rate hedging products implemented or under consideration.

4. The Finance Director is designated as the individual responsible for negotiating financial products and coordinating investment decisions for debt structure. The Finance Director is designated as the individual responsible for recommending debt and investment structures to the Council.

## **VII. Capital Improvements Policy**

### **1. Capital Improvements Plan**

The City of Pecos adopts a Capital Improvement Plan (CIP) that provides for all improvements needed for the upcoming six year period. The first year of the CIP is the Capital Improvement Budget (CIB), which communicates timing and costs associated with constructing, staffing, maintaining, and operating publicly financed facilities and improvements with a total cost over \$100,000, for the upcoming fiscal year.

a.) The City will update and re-adopt annually a six-year CIP which projects capital needs and details the estimated costs, description and anticipated funding sources for capital projects for the upcoming six year period. Projects included within the six year program must have sound cost estimates, an identified site, and verified financing sources, as well as confirmation it can be operationally staffed and maintained within the budget resources. The purpose of the Capital Improvement Plan is to systematically identify, plan, schedule, finance, track and monitor capital projects to ensure cost-effectiveness as well as conformance to established policies. No capital project shall be funded unless operating impacts have been assessed and the necessary funds can be reasonably anticipated to be available when needed. A separate CIP will be developed for the General, Water, and Sewer, Vehicle, and Landfill Funds.

b.) The annual update of the CIP will be conducted in conjunction with the annual operating budget process.

c.) The first year of the six-year CIP will be the basis of formal fiscal year appropriations during the annual budget process.

d.) The City expects to see new capital items generally first appear in the last year of the CIP.

e.) The City Manager/Finance Director will annually submit a financially balanced, multi-year Capital Improvement Plan for review by the City Council pursuant to the timeline established in the annual budget preparation schedule. The Capital Improvement Plan will incorporate a methodology to determine project priority according to developed criteria.

The Capital Improvement Plan shall provide:

o A statement of the objectives of the Capital Improvement Plan, including the relationship with the City's General Plan, department master plans, necessary service levels, and expected facility needs, as appropriate.

o An implementation program for each of the capital improvements that provides for the coordination and timing of project construction among various City departments.

o An estimate of each project's costs, anticipated sources of revenue for financing the project, and an estimate of the impact of each project on City revenues and operating budgets. Each project will include an analysis of potential risks and opportunities associated with the timing of and operations related to the project.

f.) The City acknowledges pay-as-you-go financing as a significant capital financing source, but will ultimately determine the most appropriate financing structure for each capital project both

on an individual basis after examining all relevant factors of the project and in conjunction with the funding of the entire CIP.

## 2. Capital Formation

a.) General fund revenue is the source for the General Fund CIP. Usage/service fees and impact fees will be utilized as a source of funds for the Enterprise Capital Funds.

b.) The General Fund Capital Reserve Fund is the funding source for pay-as-you-go financing and for debt service payments for debt financed projects in the General Fund CIP.

c.) Given the historical volatility of the state and other revenues, the six year projections of revenue used to complete the CIP shall be very conservative.

## 3. Fixed Assets

a.) The capitalization threshold for fixed assets shall be \$5,000. The threshold will be applied to individual fixed assets and not to groups of fixed assets. Fixed assets will only be capitalized if they have a useful life of at least one year following the date of acquisition. A physical inventory of capitalized fixed assets will be performed, either simultaneously or on a rotating basis, so that all fixed assets are physically accounted for at least once every four years.

## **VIII. Debt Policy**

1. Debt will only be incurred for financing capital assets that, because of their long-term nature or because of budgetary restraints, cannot be acquired from current or budgeted resources. Debt will not be used for operational needs. Debt financing can include general obligation bonds, revenue bonds, certificates of participation, lease/purchase agreements, special obligation bonds, or any other financing instrument allowed under Texas law.

2. The City will seek to structure debt and to determine the best type of financing for each financing need based on the flexibility needed to meet project needs, the timing of the project, taxpayer or rate payer equity, and the structure that will provide the lowest interest cost in the circumstances.

3. Debt financing will be considered in conjunction with the approval by the Council of the City's CIP.

4. Capital projects financed through the issuance of bonds, installment financings or lease financings will be financed for a period not to exceed the expected useful life of the project.

a.) General fund debt will normally have a term of 20 years or less. When practical, the term of non-Utility debt will not exceed 30 years.

b.) Enterprise fund (water and sewer) debt will normally have a term of 30 years or less. When practical, the term of Utility debt will not exceed 40 years.

5. The City will strive to maintain a high level of pay-as-you-go financing for its capital improvements.

## 6. Debt Affordability

a.) Total General Fund debt service will not exceed any limits imposed by the State. As a guide, formulas established by rating agencies will be monitored and appropriately applied by the City. Debt service as a percentage of the operating budget will be targeted at less than 15%.

b.) The City will strive to achieve amortization of 60% or more of its non-Utility debt principal within ten years.

7. The City will seek to structure debt in the best and most appropriate manner to be consistent with the Asset – Liability Management section of this policy.

8. If the City issues Revenue Bonds, and whereas the minimum coverage ratio expected for City revenue bonds is 1.20 times, upon the calculation of a coverage ratio for any Utilities System Revenue Bonds which is below 1.5 times (Net Revenues as defined by the General Indenture, but excluding cash receipts from special assessments, over Debt Service as defined by the General Indenture), the Finance Director will notify the Council of such. Within three months of such notification, the Finance Director will again report to the Council and will have performed the necessary internal study to advise the Council on the actions necessary to restore the coverage ratio to above 1.5 times. This policy is intended to ensure that all reasonable steps necessary are taken to begin the process of reviewing water revenues and rates well before the coverage ratio for outstanding revenue bonds could reach the minimum level of 1.20 times.

9. The City will seek to employ the best and most appropriate strategy to respond to a declining interest rate environment. That strategy may include, but does not have to be limited to, delaying the planned issuance of fixed rate debt, examining the potential for refunding of outstanding fixed rate debt, and the issuance of variable rate debt. The City will seek to employ the best and most appropriate strategy to respond to an increasing interest rate environment. That strategy may include, but does not have to be limited to, the issuance of variable rate debt (a historically lower interest cost), and the use of forward delivery fixed rate debt.

10. The City will monitor the municipal bond market for opportunities to obtain interest rate savings by refunding by forward delivery, currently refunding or advance refunding outstanding debt. The estimation of net present value savings for a traditional fixed rate refunding should be, at a minimum, 3% of the refunded maturities before a refunding process begins.

11. The City will strive for the highest possible bond ratings in order to minimize the City's interest costs.

12. The City will normally obtain two debt ratings (Fitch Ratings, Moody's, or Standard & Poor's) for all publicly sold debt issues.

13. While some form of outstanding debt exists, the City will strive to have a portion of that debt in the form of general obligation debt, when fiscally advantageous.

14. For all years that the City has any publicly sold debt outstanding, the City will provide annual information updates to each of the debt rating agencies if desired by those agencies.

15. The City will use the Comprehensive Annual Financial Report as the disclosure document for meeting its obligation under SEC Rule 15c2-12 to provide certain annual financial information to the secondary debt market via various information repositories.

16. The City recognizes the significance of the debt portfolio and the need for the ability to properly manage and maintain that portfolio. The Finance Director will maintain a current database of all debt, and provide an annual review of the debt strategy to Council.

### **IX. Accounting, Auditing and Financial Reporting**

1. The City will maintain accounting systems in compliance with recognized industry standards. The City will maintain accounting systems that enable the preparation of financial statements in conformity with generally accepted accounting principles (GAAP).

a.) The basis of accounting within governmental funds will be modified accrual.

b.) The basis for accounting within all Enterprise and Internal Service Funds will be full accrual.

2. Financial systems will be maintained to enable the continuous monitoring of revenues and expenditures or expenses with complete sets of monthly reports provided to the Council and the City Manager. Monthly expenditure/expense reports will be provided to each department head for their functional area and direct access to the financial system will be made available to department heads and other staff as much as practical and its use encouraged.

3. The City will place emphasis on maintenance of an accounting system which provides strong internal budgetary and financial controls designed to provide reasonable, but not absolute, assurance regarding both the safeguarding of assets against loss from unauthorized use or disposition and the reliability of financial records for preparing financial statements and reports, as well as the accountability of assets.

4. An annual audit will be performed by an independent certified accounting firm which will issue an opinion on the annual financial statements.

5. The City will solicit proposals from qualified independent certified public accounting firms for audit services. The principal factor in the audit procurement process will be the auditor's ability to perform a quality audit. The City may enter into a multiyear agreement with the selected firm for a period of up to three fiscal years. Firms are not barred from consecutive contract awards. The Council, upon recommendation from the City Manager and Finance Director shall approve the contractual relationship with the auditor.

6. The Finance Director will conduct some form of internal audit procedures at least one time per year, specifically focusing upon, but not limited to, cash receipts procedures.

7. The City will prepare a CAFR in compliance with established criteria to obtain the Government Finance Officers Association's Certificate of Achievement for Excellence in Financial Reporting and will be submitted to that award program each year.

8. Full and complete disclosure will be provided in all regulatory reports, financial statements and debt offering statements.

10. The City shall use the CAFR as the disclosure document for meeting its obligation to provide certain annual financial information to the secondary debt market via various information repositories. The

annual disclosure is a condition of certain debt covenants and contracts that are required by SEC Rule 15c2-12.

11. The Finance Director will develop and maintain a Financial Procedures Manual as a central reference point and handbook for all financial, accounting and recording procedures.

12. The Information Technology Director will establish, document and maintain a Computer Disaster Recovery Plan and will provide for the daily backup of data and the offsite storage of the same. This Plan will be integrated with the City's Emergency Management Plan.

## **X. Cash Management Policy**

### 1. Receipts

a.) All aspects of cash receipts shall be subject to proper internal controls with standard controls documented and followed by revenue generating departments.

b.) The Finance Director, with approval of the City Manager, shall prescribe internal control procedures for departments which address adequate segregation of duties, physical security, daily processing and reconciliation, use of automated resources, and treatment of overpayments.

c.) Cash receipts will be collected as expediently as reasonably possible to provide secure handling of incoming cash and to move these monies into interest bearing accounts and investments.

d.) All incoming funds will be deposited daily as required by State law.

e.) The Finance Director is responsible for conducting at least two unannounced random or risk based internal audits of cash receipting locations per fiscal year.

f.) Upon any suspicion of fraud, the department head shall immediately notify the City Manager for further investigation.

g.) Upon any suspicion of non-compliance with internal control directives, the department head shall immediately notify the City Manager for further investigation.

### 2. Cash Disbursements

a.) Disbursements will be made timely in advance of or on the agreed-upon contractual date of payment unless earlier payment provides greater economic benefit to the Town.

b.) Inventories and supplies will be maintained at minimally appropriate levels for operations in order to increase cash availability for investments purposes and allow for greater controls; reducing risks.

c.) Dual signatures are required for City checks. Use of secured electronic signature is acceptable.

d.) Electronic payments shall be utilized to the fullest extent possible where it is determined to be cost effective by the Finance Director. Such payments shall be integrated with financial systems and shall follow the proper internal controls.

## **XI. Investment Policy**

1. Policy - It is the policy of the City to invest public funds in a manner which will provide the highest investment return with the maximum security while meeting the daily cash flow requirements of the City and conforming to all State statutes governing the investment of idle funds.

2. Scope - This investment policy applies to all financial assets of the City except authorized petty cash, and debt proceeds, which are accounted for and invested separately from pooled cash. The City pools the cash resources of its various funds and participating component units into a single pool, as deemed appropriate, in order to maximize investment opportunities and returns. Each fund's and participating component unit's portion of total cash and investments is tracked by the financial accounting system.

3. Prudence

a.) The standard of prudence to be used by authorized staff 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 would 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.

b.) Authorized staff acting in accordance with procedures and this investment policy and exercising due diligence shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion to the Council and the liquidity and the sale of securities are carried out in accordance with the terms of this policy.

4. Authorized Staff – The Finance Director will establish and maintain procedures for the operation of the investment program that are consistent with Industry wide standards. Such procedures will include delegation of authority to persons responsible for investment transactions. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the Finance Director. The Finance Director will be responsible for all transactions undertaken and will establish and maintain a system of controls to regulate the activities of subordinates. In the absence of the Finance Director and those to which he or she has delegated investment authority, the City Manager or his or her designee is authorized to execute investment activities.

5. Objectives - The City's objectives in managing the investment portfolio, in order of priority, are safety, liquidity, and yield.

a.) Safety - 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. To best mitigate against credit risk (the risk of loss due to the failure of the security issuer) diversification is required. To best mitigate against interest rate risk (the risk that changes in interest rates will adversely affect the market value of a security and that the security will have to be liquidated and the loss realized) the second objective, adequate liquidity, must be met.

b.) Liquidity - The investment portfolio shall remain sufficiently liquid to meet all operating and debt service cash requirements that may be reasonably anticipated. The portfolio will be structured so that securities mature concurrent with cash needs (static liquidity), with securities with an active secondary market (dynamic liquidity), and with deposits and investments in highly liquid money market and mutual fund accounts.

c.) Yield - The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary, economic and interest rate cycles, taking into account investment risk constraints and liquidity needs.

6. Ethics and Conflicts of Interest - Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with the proper execution and management of the investment program, or that could impair their ability to make impartial decisions. Employees and investment officials shall disclose to the City Manager any interests in financial institutions with which they conduct business material to them. They shall further disclose any personal financial or investment positions that could be related to the performance of the investment portfolio. Employees and officers shall refrain from undertaking personal investment transactions with the same individuals with whom business is conducted on behalf of the City.

#### 7. Authorized Financial Dealers and Financial Institutions

a.) The Finance Director will maintain a list of financial institutions that are authorized to provide investment services.

b. Any financial institutions and broker dealers that desire to become qualified to conduct investment transactions with the City must supply the Finance Director with the following:

- 1.) Audited financial statements; ° Proof of National Association of Securities Dealers certification; 2.) Proof of State registration; and 3.) Certification of having read the City's investment policy.

c.) Any previously qualified financial institution that fails to comply or is unable to comply with the above items upon request will be removed from the list of qualified financial institutions.

d.) The Finance Director shall have discretion in determining the number of authorized financial institutions and may limit that number based upon the practicality of efficiently conducting the investment program. The Finance Director shall also have the discretion to add or remove authorized financial institutions based upon potential or past performance.

8. Internal Control - The City Manager is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the entity 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 the cost of a control should not exceed the

benefits likely to be derived and that the valuation of costs and benefits requires the use of estimates and judgments by management.

9. Collateralization - Collateralization is required for all cash bank deposits.

10. Delivery and Custody - All investment security transactions entered into by the City shall be conducted on a delivery versus payment basis. Securities will be held by a third party custodian designated by the Finance Director and each transaction will be evidenced by safekeeping receipts and tickets.

11. Authorized Investments - The City is empowered to invest in certain types of investments. The City Council approves the use of the following investment types:

a.) Obligations of the United States or obligations fully guaranteed as to both principal and interest by the United States.

b.) Obligations of the Federal Financing Bank, the Federal Farm Credit Bank, the Federal Home Loan Banks, the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, the Government National Mortgage Association, the Federal Housing Administration, and the United States Postal Service.

c.) Fully collateralized cash deposits and interest or certificates of deposit with any bank.

d.) Prime quality commercial paper bearing the highest rating of at least one nationally recognized rating service, which rates the particular obligation. Participating shares in a mutual fund for local government investment.

12. Prohibited Forms of Authorized Investments

a.) The use of repurchase agreements in the normal investment portfolio (not debt proceeds) is prohibited.

b.) The use of collateralized mortgage obligations is prohibited.

c.) The use of any type of securities lending practices is prohibited.

13. Selection of Securities - The Finance Director or his or her designee will determine which investments shall be purchased and sold and the desired maturity date(s) that are in the best interest of the City. The selection of an investment will involve the evaluation of, but not limited to, the following factors: cash flow projections and requirements; current market conditions; and overall portfolio balance and makeup.

14. Active Trading of Securities -It is the City's intent, at the time of purchase, to hold all investments until maturity to ensure the return of all invested principal. However, if economic or market conditions change making it in the City's best interest to sell or to trade a security before maturity, that action may be taken.

15. Pooled Cash and Allocation of Interest Income - All monies earned and collected from investments other than bond proceeds will be allocated monthly to the various participating funds and component units based upon the average cash balance of each fund and component unit as a percentage of the total pooled portfolio. Earnings on bond proceeds will be directly credited to the same proceeds.

16. Marking to Market - A report of the market value of the portfolio will be generated at least semi-annually by the Finance Director. The Finance Director will use the reports to review the investment portfolio in terms of value and price volatility, as well as for compliance with GASB Statement #31.

17. Software - The City recognizes the significance of the size of its investment portfolio and of the requirements contained in this policy. The City will utilize investment software which enables efficient transaction processing and recording, sufficient portfolio monitoring and the ability to maintain reporting compliance with this policy.

18. Reporting - The Finance Director will prepare a quarterly investment report that will be submitted with the Council's monthly report package.

## **XII. Review and Revision**

The City will formally review this set of financial and budgetary policies at least once every three years.