



# INVESTMENT POLICY DEVELOPMENT

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## 2 GTOT CHECKLIST

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- Objectives

- Understand the difference between required elements of an investment policy under PFIA and “best practice”
- Understand the 2017 legislative changes to PFIA and how to incorporate them into the policy
- Understand other regulatory influences on investment policy maintenance

### 3 GTOT CHECKLIST

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## Policy Statement

- “invest in a manner which will provide the highest rate of return with the maximum security”
- “invest in a manner that will provide security and optimize interest earnings to the maximum extent possible”

# 4 GTOT CHECKLIST

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## Scope

Should all funds be included in the investment policy?

- Non-profit corporations
- Deferred compensation and retirement funds
- Endowment/donated funds
  - If separately managed under specified terms of use
- Funds governed by additional authority (bond funds)

Pooled or separately invested?

“All funds are managed as a pooled fund group, referenced in this Policy as the City’s investment pool, with the exception of the following, which are managed as separately invested assets.”

# 5 GTOT CHECKLIST

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## General Objectives

- Watch for inconsistent objectives/guidelines!
  - Example: Maximum maturity for individual investments inconsistent with maximum weighted average maturity for pool
- Procedures to monitor investment ratings and to liquidate if necessary
  - Monitoring through recognized financial information sources (rating agency sites)
  - “All prudent measures consistent with PFIA shall be taken to liquidate an investment that no longer has the minimum rating required by PFIA.”

## 6 GTOT CHECKLIST

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### Prudent Person Rule

- Include PFIA language protecting investment officers in addition to prudent person standard
- “...the governing body of the investing entity retains ultimate responsibility as fiduciaries of the assets of the entity”
- Determination of prudence based on the investment of all funds and consistency with the written investment policy

# 7 GTOT CHECKLIST

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## Capability of Investment Management

- Suggested language: *The City shall provide periodic training in investments for the investment personnel through courses and seminars offered by professional organizations and associations in order to insure the quality and capability of the City's investment personnel making investment decisions in compliance with the PFIA.*

# 8 GTOT CHECKLIST

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## Ethics Disclosure and Conflicts of Interest

- PFIA requirements apply to investment officers
- “Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions.”

## Delegation of Investment Authority

- If not included in the investment policy, attach a copy of resolution

# 9 GTOT CHECKLIST

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## Investment Training

- Know the difference between state agency and local government requirements
  - Two-year training period consistent with local government's fiscal year
- Does the policy include the correct number of training hours?
  - 10 hours of ongoing training reduced to 8 hours every two years for city and school district investment officers
- Are the independent sources of investment training included in the investment policy?
  - If not, request a copy of the resolution

# 10 GTOT CHECKLIST

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## Investment Policy Certification Form

- Most common errors
  - Outdated language
  - Example: “preclude imprudent activities” instead of the more narrow “preclude transactions that are not authorized by the policy”
  - Example: “registered principal” as the required signatory of the certification instead of “qualified representative

# II GTOT CHECKLIST

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## Qualified Bidders List

- Most common errors
  - Applying to all business organizations, including banks and investment pools
  - Not acknowledging in the policy that either the governing body or a designated investment committee approves the list followed by an annual review
  - Assigning responsibility for approving the list either to the CEO or the CFO

# 12 GTOT CHECKLIST

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## Independent Third-Party Safekeeping

- Most common errors
  - Not addressing this “best practice”
  - Not applying to both securities owned by the investing entity and to collateral pledged to the investing entity
  - Not requiring a written agreement among the parties

## Delivery vs. Payment

- Must be included in investment policies

# 13 GTOT CHECKLIST

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## Competitive Bidding

- Most common errors
  - Not addressing this “best practice”
  - Should be addressed if the investing entity includes securities on the list of authorized investments
  - Should be addressed if there is a need to establish that a market price was received in the investment of bond proceeds
  - Establish exceptions for certain types of transactions
    - Certificate of deposit included in the depository contract

# 14 GTOT CHECKLIST

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## Suitable and Authorized Investments

- Most common errors
  - Outdated requirements such as restricting banks eligible to provide certificates of deposit to those “domiciled in Texas”
  - Not including the required ratings for investment types
  - Requiring a rating without considering appropriate exceptions
  - Not including all investment types in the list of authorized investments, including those used for sweep accounts and bond proceeds
  - Not including all investment types in the list of authorized investments in the application for GTOT investment policy certification

# 15 GTOT CHECKLIST

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## Prohibited Investments

### Effect of Loss of Required Rating

- Moved to “General Objectives”
- “The City shall take all prudent measures consistent with ~~(this Policy)~~ the Act to liquidate an investment that does not have the minimum rating required by the Act.”

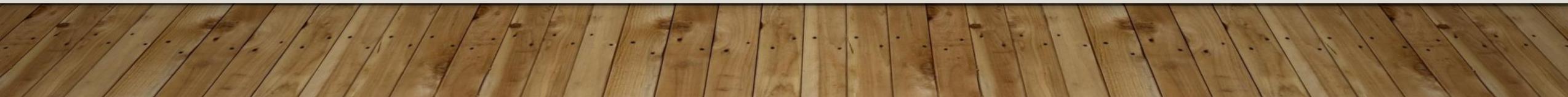
# 16 GTOT CHECKLIST

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## Collateral Policy – Most Common Errors

- Not addressing this requirement of the Public Funds Collateral Act, Chapter 2257, Government Code
- Not addressing all aspects of collateral management, i.e., margin, frequency of valuation, substitution procedure, eligible securities, etc.
- Limiting eligible collateral to authorized investments in the Policy

## Diversification and Maximum Maturities

- Is it enough to declare that diversification is a goal, or must we practice what we preach?
  - Is action required if limits are exceeded?
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# 17 GTOT CHECKLIST

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## Investment Strategies

- Weakest part of investment policies
- Check for inconsistency with the policy
  - Investment maturities shall be staggered throughout the budget cycle” but almost 100% is invested in pools
  - Strategy statement includes an investment not on the authorized list (ex.: flexible repurchase agreement)
  - Strategy statement too generic

# 18 GTOT CHECKLIST

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## Weighted Average Maturity for Pooled Fund Groups

- Does the policy include a statement that funds are/are not pooled?
- WAM is required if funds are pooled

## Quarterly Investment Reporting

- Refer to PFIA requirements instead of listing in the Policy

# 19 GTOT CHECKLIST

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Review by Independent Auditor

Marking to Market

- Methods to monitor the market price of investments
- Watch for statements such as “market value shall be obtained from one of the approved brokers”

# 20 GTOT CHECKLIST

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## Internal Controls

- PFIA compliance audit requirement
- Establishment of internal controls
  - Assign responsibility for creating, implementing and maintaining an internal control system

## Exemption for Existing Investments

## Annual Review and Adoption of Investment Policy and Strategies

## 21 PUBLIC FUNDS INVESTMENT ACT COMPLIANCE

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- Annual approval of Investment Policy by Governing Board
- Investment strategy included with investment policy
- Quarterly reporting of investment cost and fair value information
- Compliance with Investment Policy regarding authorized and unauthorized investments (considering diversification requirements)
- Designated investment officers meeting continuing professional education requirements (many training budgets have been trimmed)
- Use of approved brokers, including review of investment policy certification

## 22 MUNICIPAL ADVISOR RULE

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Effective July 1, 2014

A municipal advisor includes any person (other than an employee of the municipality) providing advice to a municipality on the issuance of municipal securities.

Persons who provide advice to a municipality on the investment of municipal bond proceeds are also considered municipal advisors.

- Professionals who provide such advice generally but are not registered as municipal advisors may request written confirmation that the sources of the municipality's investments do not include proceeds of bonds or other municipal securities

## 23 SEC MONEY MARKET MUTUAL FUND REFORM

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SEC-approved reforms became effective October 2016

- Created a division between institutional prime and tax-exempt funds and the rest of the MMMF's by allowing a floating NAV and a combination of fees-gates
  - MMMF's that did not seek to maintain a \$1.00 NAV were no longer authorized investments under PFIA
- GASB issued final guidance on local government investment pools
  - Pools continued to report investments on an amortized cost basis

## 24 LIQUIDITY COVERAGE RATIO

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The Federal Reserve Board and the FDIC finalized a rule in September 2014 to strengthen the liquidity positions of large financial institutions, called the Liquidity Coverage Ratio or LCR

- Hold high quality, liquid assets (HQLA) that can be converted easily and quickly into cash in an amount equal to or greater than its projected cash outflows minus its projected cash inflows during a 30-day stress period
- HQLA does not include municipal securities

# 25 85<sup>TH</sup> TEXAS LEGISLATIVE SESSION – PFIA CHANGES

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## Authorized Investments

- Money market mutual funds (HB 1003)
  - Reauthorizes “prime” money market mutual funds by removing the maintenance of a \$1.00 NAV as a stated objective of the fund and the requirement of having a 90-day weighted average stated maturity
    - Substitutes compliance with SEC Rule 2a-7
  - May authorize some ultra-short bond funds
    - May not be eligible for investment of bond proceeds and bond-related funds such as reserve and debt service funds

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## Authorized Investments and Training

- Local government investment pools (HB 1003)
  - Allows a pool to use either amortized cost or fair value accounting
  - Requires the pool to stabilize at \$1.00 NAV.
- Hedging agreements (HB 1003)
  - For entities with at least \$250 million in outstanding debt
- Investment training hours (HB 1238)

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## Investment Policies (HB 1701)

- Public entities are only required to present their investment policies to local government investment pools
- Consider providing your approved list with copies of your approved investment policy
  - FINRA’s “Know Your Customer” rules were established based on the suitability requirements of FINRA Rule 2111

# 28 85<sup>TH</sup> TEXAS LEGISLATIVE SESSION – PFIA CHANGES

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## Authorized Investments

- Interest-bearing bank deposits that are insured by FDIC or NCUS Insurance Fund (HB 1003 and HB 2647)
- Federal Home Loan Bank obligations (HB 2928)
  - Clarifies that FHLB obligations are authorized investments
  - Clarifies that FHLB Letter of Credit is eligible as collateral for certificates of deposit by referring to Chapter 2257, Government Code (Collateral Act)
- Divestiture (SB 253)