

MEMORANDUM

TO: Honorable Mayor and City Council

FROM: John J. McCue, City Manager

DATE: April 1, 2008

SUBJECT: Revised Investment Plan

The current investment plan was adopted in 1998 and has not been reviewed or revised since its original adoption and requires a major overhaul.

Attached you will find two documents; one document is the current investment plan (4 pages), and the second document is the proposed replacement investment plan (7 pages). The Government Finance Officers Association (GFOA) created a sample investment plan to aid in the preparation of an investment plan. The sample plan was not intended to supplant an existing plan; rather, it was presented as a model to help investing entities customize a plan to fit their particular needs, constraints and capabilities. The proposed Investment Plan was modeled using the GFOA's recommendations.

Because the size of the City's investment portfolio is less than \$10 million it is not a fiscally viable option to retain an investment broker in order to access many of the authorized investment tools available within the Investment Plan. As the City's annual operating budget grows, so will the City's investment portfolio. The investment plan as proposed will allow the city to access other investment options as the size of the portfolio increases, without the need to amend the Investment Plan.

Currently, the City's surplus funds are diversified between Wachovia (sweep accounts), BB&T (money market savings accounts) and the State Board of Administration (Local Government Invest Pool), all of which are authorized investments in the existing plan and all will remain authorized investments in the proposed investment plan.

The proposed process for updating and approving the new investment plan is as follows: 1) Workshop to discuss the proposed Investment Plan, 2) presenting the approved Investment Plan with an ordinance for adoption by Council and 3) staff will present recommendations to Council regarding investment strategies.

Staff requests that the Council review the proposed plan in preparation for the Investment Plan Workshop, scheduled for April 8th from 6-7 pm. As you prepare for the workshop, please feel free to contact me or Christine with any questions or concerns.

City of Orange City
April 2008

ARTICLE V. INVESTMENT PLAN

Sec. 2-181. Scope

This investment plan shall apply to funds under the control of the City of Orange City, Florida (hereinafter "City") in excess of those required to meet current expenses. This investment policy shall not apply to pension funds, including those funds in Florida Statutes chapters 175 and 185. Nor shall this investment plan apply to funds related to the issuance of debt where there are other existing policies or indentures in effect for such funds, however, absent such other controlling documents this plan shall apply to such funds. The City Manager or designee will consolidate, where practicable and allowable, for the purposes of investment, cash balances and investments from all funds covered by this policy to maximize investment earnings and reduce risks. The investment of funds shall comply with all controlling state statutes, ordinances and covenants covering the City's investments.

Sec. 2-182. General Objectives

The primary objectives, in priority order, of investment activities shall be safety, liquidity, yield and transparency:

(1) Safety and Legality - Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks the preservation of capital in the overall portfolio. The objective will be to limit credit risk and interest rate risk to a level commensurate with the risks associated with prudent investment practices and performance benchmarks, if applicable.

A. Credit Risk - The City will limit credit risk, the risk of loss due to the failure of the security issuer or backer, by diversifying the investment portfolio so that potential losses on individual securities will be minimized and by limiting investments to specified credit ratings.

B. Interest Rate Risk - The City will minimize the risk that the market value of securities in the portfolio will fall due to changes in general interest rates by limiting the maximum duration of the portfolio to 3 years.

(2) Liquidity - 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 securities mature to meet anticipated demands (static liquidity). Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets (dynamic liquidity). The portfolio may be placed in local government investment pools or money market mutual funds that offer same-day liquidity for short-term funds.

(3) Yield - The investment portfolio shall be designed with the objective of attaining a market rate of return, as measured by specified benchmarks, 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. The core investments are limited to relatively low-risk securities in anticipation of earning a fair return relative to the risk being assumed. Securities shall not be sold prior to maturity with the following exceptions:

A. A security with declining credit may be sold early to minimize loss of principal.

B. A security swap that would improve the quality, yield, or target duration in the portfolio.

C. Liquidity needs of the portfolio require that the security be sold.

(4) Transparency – The City shall operate its portfolio in a transparent manner, making its periodic reports both available for public inspection and designed in a manner which communicates clearly and fully information about the portfolio, including market pricing, adjusted book value, yields, and Committee on Uniform Security Identification Procedures (CUSIPs) of various securities.

Sec. 2-183. Standards of Care

(1) Prudence - The standard of prudence to be used by investment officials shall be the Prudent Person Rule and shall be applied in the context of managing an overall portfolio. City personnel, acting in accordance with 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 to the City's governing board in a timely fashion and the liquidity and the sale of securities are carried out in accordance with the terms of this policy.

The Prudent Person Rule states that: "Investments should 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 from the investment."

(2) Ethics and Conflicts of Interest – The City Manager or designee 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. These investment officials shall disclose annually, in a written statement, 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. They shall refrain from undertaking personal investment transactions with the same individual(s) with whom business is conducted on behalf of the City.

(3) Delegation of Authority - Authority to manage the investment program is granted to the City Manager or designee and other authorized personnel. Additional authorized personnel include any other person or position approved by the City's governing board. The City may seek professional advice and therefore may contract with a federally registered investment advisory firm that specializes in public funds fixed income management. No person may engage in an investment transaction except as provided under the terms of this policy. The City Manager or designee shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

Sec. 2-184. Broker Dealers, Safekeeping and Custody

(1) Authorized Financial Dealers and Institutions – The City shall list financial institutions consisting of banks and other depository institutions authorized to provide depository and investment services. In addition, a list will be maintained of approved security broker/dealers consisting of "primary" dealers or regional dealers that qualify under Securities and Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule). Both lists shall be reviewed by the City Manager or designee at least annually.

(2) Annual Review - An annual review of the financial conditions and registration of qualified financial institutions and broker/dealers will be conducted by the City Manager or designee and/or Investment Advisor under the direction of the City. The distribution of trading among the approved broker/dealers of securities which at the time of purchase had maturities greater than seven (7) days shall be reported annually to the City Council.

(3) Delivery vs. Payment - Securities transactions between a broker-dealer and the safekeeping agent or custodian involving purchase or sale of securities by transfer of money or securities must be made on a "delivery vs. payment" basis, if applicable, to ensure that the custodian will have the security or money, as appropriate, in hand at the conclusion of the transaction.

(4) Safekeeping, Custody and Perfection of Interest - Securities shall be held with a third party; and all securities purchased by, and all collateral obtained by, the unit of local government should be properly designated as an asset of the unit of local government. No withdrawal of securities, in whole or in part, shall be made from safekeeping or custody, except by an authorized staff member of the unit of local government.

Sec. 2-185. Suitable and Authorized Investments

This investment plan is authorized by the City Council. Investments not listed in the investment plan are prohibited.

The investment portfolio shall be structured in such manner as to provide sufficient liquidity to pay obligations as they come due. To that end, the investment plan should direct that, to the extent possible, an attempt will be made to match investment maturities with known cash needs and anticipated cash-flow requirements.

Prior to conducting transactions as authorized by this plan the City Manager or designee shall determine the approximate maturity date based on cash-flow needs and market conditions, analyze and select one or more optimal types of investment, and competitively bid the security in question when feasible and appropriate. Except as otherwise required by law, the bid deemed to best meet the investment objectives shall be selected.

Consistent with the Florida Statutes the following investments will be permitted by this policy:

(1) **Authorized Issuers** - The criteria for authorized investments is broken down into four sections. Each investment must comply with the provisions of each section. These sections address who can issue authorized investments, what minimum credit ratings these investments must have, what maturity or other limitations apply concerning interest rate risk, and how much of any security may be held. Subject to additional restrictions in this Part V, securities may be held that are issued by:

A. The United States Treasury and Agency securities - Securities that are issued by the United States Treasury or those for which the full faith and credit of the United States government guarantees fully all principal and interests payments.

B. Government Sponsored Enterprises (GSE) - Securities issued by the Federal Farm Credit Bank, the Federal Home Loan Mortgage Corporation, the Federal Home Loan Bank, the Federal National Mortgage Association, or the Federal Agricultural Mortgage Corporation. Any other GSE shall be considered as corporate debt for the purposes of this Policy and shall be authorized under the criteria set forth in D. Corporations (below).

C. State and Local Governments - General or revenue obligation of any state of the United States, the District of Columbia, or any territorial possession of the United States, or, of any political subdivision, institution, department, agency, instrumentality, or authority of any of such governmental entities.

D. Corporations - United States dollar-denominated debt instruments issued by a corporation or bank which is organized and operated within the United States.

E. Local Government Investment Pools - Shares in local government investment pools organized under Chapter 163, Part I, Florida Statutes.

F. The State Board of Administration pool (SBA). Shares in the SBA pool organized under Chapter 218, Part IV, Florida Statutes.

G. Money Market Mutual Funds - Shares of any money market fund that is registered as an investment company under the federal "Investment Company Act of 1940", as amended.

H. Repurchase Agreements - Securities referred to in paragraph A or B of this Section (1) and that can otherwise be purchased under this plan may be subject to a Repurchase Agreement. Such securities subject to this agreement must have a coupon rate that is fixed from the time of settlement until its maturity date, and must be marketable. Such securities must be delivered to the entity or to a third-party custodian or third-party trustee for safekeeping on behalf of the public entity. The collateral securities of any repurchase agreement must be collateralized at no less than one hundred two percent and marked to market no less frequently than weekly. All approved institutions and dealers transacting repurchase agreements shall execute and perform as stated in the Master Repurchase Agreement. All repurchase agreement transactions shall adhere to the requirements of the Master Repurchase Agreement.

No City funds shall be invested in any security issued by entities authorized in this Section (1) on which the coupon rate (or a schedule of stepped fixed coupon rates) is not fixed from the time the security is settled until its maturity date, other than shares in qualified money market mutual funds or local government investment pool, unless the coupon rate is: (a) Established by reference to the rate on a United States treasury security with a maturity of one year or less, or to the United States dollar London Interbank offer rate of one year or less maturity, or to the cost of funds index or the prime rate as published by the federal reserve; and (b) Expressed as a positive value of the referenced index plus or minus a fixed number of basis points. A municipal index may be used for the investment of bond or note accounts from issues with coupons linked to the same index. For purposes of this section, "maturity date" means the last possible date, barring default, that principal can be repaid to the purchaser.

(2) **Credit Ratings** - Securities may be purchased if at the time of purchase the securities meet the following credit quality criteria:

A. United States Treasury and Agency securities – Ratings are not required for U.S. Treasury securities. Agencies backed by the full faith and credit of the United States government, such as Government National Mortgage Association (GNMA), must have at least two AAA/Aaa/AAA long-term credit ratings from Standard & Poor's, Moody's or Fitch, respectively. Neither Standard & Poor's, Moody's nor Fitch may rate this security below AAA/Aaa/AAA, respectively, otherwise any security below this rating shall for the purposes of this Policy be treated as Corporate debt subject to the restrictions of Sections 2-182.-184. of this Article V.

B. Government Sponsored Enterprises (GSE) - Authorization of the listed GSE in paragraph B of Section 1 is predicated upon these institutions maintaining at least two AAA/Aaa/AAA long-term credit ratings from Standard & Poor's, Moody's or Fitch, respectively. Should any of these credit rating agencies assign a long-term credit rating to any listed GSE below AAA/Aaa, the GSE shall be considered as corporate debt subject to the restrictions of Sections 2-182.-184. of this Article V.

C. State & Local Governments - At the time of purchase, such securities must carry at least two long-term credit rating of AAA/Aaa/AAA from Standard & Poor's, Moody's or Fitch, respectively and neither Standard & Poor's, Moody's nor Fitch may rate this security below AAA/Aaa/AAA, respectively. If the AAA/Aaa/AAA credit rating was achieved via some form of third party credit enhancement, then the underlying issuer must have two long-term credit rating none of which may be below AA-/Aa3/AA- from Standard & Poor's, Moody's or Fitch, respectively.

D. Corporations - At the time of purchase, all non-money market instruments must carry at least two long-term credit rating from Standard & Poor's, Moody's or Fitch, respectively, and neither Standard & Poor's, Moody's nor Fitch may rate this instrument below AAA/Aaa/AAA, respectively. For money market instruments, which comply with SEC Rule 2a-7 at the time of purchase, such securities must carry at least two short-term credit ratings and no short-term credit rating may fall below A1+ from Standard & Poor's, P1 from Moody's, or F1+ from Fitch.

Should a security's credit rating drop below these standards after purchase, the City's authorized personnel shall act as Prudent Persons, in managing the risks associated with this security, and shall immediately notify the City's governing board of such an event.

E. Local Government Investment Pools - At the time of purchase, local government investment pool must carry a AAAM rating from Standard & Poor's.

F. Money Market Mutual Funds - At the time of purchase, money market fund must carry a AAAM rating from Standard & Poor's.

G. Repurchase Agreements - At the time of purchase the counter-party to any such agreements must carry short-term credit ratings which conform to those required by paragraph D of this section (2).

H. Deposits in State Qualified Public Depositories (QPD) - Banks deposits for the City must comply with Chapter 280.16 Florida Statutes. Such deposits in QPD must be collateralized according to the statutory requirements.

(3) Interest Rate Risk Restrictions - Securities may be purchased if at the time of purchase the securities meet the following credit quality criteria:

A. The United States Treasury and Agency securities backed by the full faith and credit of the United States government - At the time of purchase, securities must have a maturity no greater than of three (3) years from the date of settlement to the maximum possible maturity date. The forward delivery period on such securities may not exceed 60 days.

B. Government Sponsored Enterprises (G.S.E.) - At the time of purchase, securities must have a maturity no greater than of three (3) years from the date of settlement to the maximum possible maturity date. The forward delivery period on such securities may not exceed 60 days.

C. State & Local Governments - At the time of purchase, such securities must have a maturity no greater than of three (3) years from the date of settlement to the maximum possible maturity date. The forward delivery period on such securities may not exceed 60 days.

D. Corporations - At the time of purchase, such securities must have a maturity no greater than three (3) years from the date of settlement to the maximum possible maturity date. The forward delivery period on such securities may not exceed 60 days.

- E. Local Government Investment Pools - At the time of purchase, shares in the local government investment pool must be fully redeemable on the next business day.
 - F. Money Market Mutual Funds - At the time of purchase, shares in the money market fund must be fully redeemable on the next business day.
 - G. Repurchase Agreements - For repurchase agreements, at the time of purchase such agreements must have a maturity no greater than one year from the date of settlement. The forward delivery period on such securities may not exceed 60 days.
 - H. Overall Portfolio Interest Rate Risk - At no time may the City purchase any security that would cause the portfolio of the City to have a duration of greater than three (3) years.
- (4) **Diversification Limits** – Chapter 218.415 (8) Florida Statutes states that the investment policy shall provide for appropriate diversification of the investment portfolio. The specific diversification guidelines for the City of Orange City will be determined based on the individual requirements of the City of Orange City.

Sec. 2-186. Internal Controls

The City Manager or designee shall establish a system of internal controls which shall be in writing and made a part of the governmental entity's operational procedures. The investment policy shall provide for review of such controls by independent auditors as part of any financial audit periodically required of the unit of local government. The internal controls should be designed to prevent losses of funds which might arise from fraud, employee error, misrepresentation by third parties, or imprudent actions by employees of the City.

Sec. 2-187. Reporting

1. Methods - The City Manager or designee shall prepare and provide to the City Council an investment report at least quarterly. The investment report shall include a breakdown of the investments, by class or type, book value, income earned, and market value as of the date of the report. Such reports shall be available to the public.
2. Performance Standards - The City's cash management portfolio shall be designed with the objective of regularly meeting or exceeding a selected performance benchmark, which could be the average return on three-month U.S. Treasury bills, the state investment pool, a money market mutual fund or the average rate of fed funds.
3. Marking to Market - The market value of the portfolio shall be calculated at least quarterly and a statement of the market value of the portfolio shall be issued at least quarterly.

Sec. 2-188. Policy Considerations & Implementation

1. Exemption - Any investment currently held that does not meet the guidelines of this policy shall be exempted from the requirements of this policy. At maturity or liquidation, such monies shall be reinvested only as provided by this policy.
2. Amendments - This policy shall be reviewed on a biannual basis. Any changes must be approved by the governing body of the City.

3. Continuing Education - Chapter 218.415 (14) Florida Statutes states that the investment policy shall provide for the local government's officials responsible for making investment decisions. The City Manager or designee shall annually complete eight (8) hours of continuing education in subjects or courses of study related to investment practices and products.

ORDINANCE NO. 98-03-01

City of Orange City

ARTICLE V. INVESTMENT PLAN*

***Editor's note:** Ord. No. 98-03-01, § 1, adopted April 14, 1998, set out provisions intended for use as art. V, §§ 2-161--2-169. In order to allow for future expansion of art. IV, and at the discretion of the editor, these provisions have been codified as 2-181--2-189.

Sec. 2-181. Introduction and scope.

It is the policy of the City of Orange City ("the city") to invest public funds in a manner so as to place highest priority on the safety of principal and liquidity. The optimization of investment returns shall be secondary to the requirements for safety and liquidity. The funds will also be invested as to meet the daily cash flow demands of the city, and conform to all federal and state statutes and city resolutions governing the investment of public funds. This investment policy applies to funds under control of the city in excess of those required to meet current short-term expenses.

The investment policy shall not apply to pension funds, trust funds or funds related to the issuance of debt where there are other existing policies or indentures in effect for such funds. These funds will be accounted for in the city's annual financial report and audit statements prepared by the city's independent auditors.

(Ord. No. 98-03-01, § 1, 4-14-98)

Sec. 2-182. Investment objectives.

It is the policy of the city to invest public funds in a manner which will provide, in order of priority:

- (1) Safety of capital;
- (2) Liquidity of funds; and
- (3) Investment income.

Investments held should be diversified to the extent practicable to control the risk of loss resulting from over concentration of assets in a specific maturity, issuer, instrument, dealer, or bank through which financial instruments are bought and sold. Diversification strategies within the established guidelines shall be reviewed at least quarterly by the investment officer and revised as necessary. The city recognizes that no investment is totally without risk and that the investment activities of the city are a matter of public record.

(Ord. No. 98-03-01, § 1, 4-14-98)

Sec. 2-183. Prudence and ethical standards.

The standard of prudence to be applied by the city's investment officer shall be the "prudent person rule", which generally states, "investments should 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 from the investment."

The city's investment officer, acting in accordance with written procedures and exercising due diligence, shall not be held personally responsible for a specific security's credit risk or market price changes, provided that these deviations are reported immediately in writing to the city council.

(Ord. No. 98-03-01, § 1, 4-14-98)

Sec. 2-184. Authorized investments.

The following are authorized investments for the city:

- (1) Insured money market or savings accounts maintained in state certified qualified public depositories, as defined in F.S. § 280.02. Sufficient funds will be kept in such accounts to cover all outstanding checks drawn on the city's demand accounts which are zero balance accounts.
- (2) Direct obligations of the U.S. Treasury such as Treasury bills, notes, and bonds issued by the United States government.
- (3) Bonds or other interest bearing obligations, the payment of the principal and interest of which is unconditionally guaranteed by the United States government.
- (4) Securities issued by, guaranteed by, or for which the credit is pledged for payment by one of the federal agencies and/or instrumentalities.
- (5) Certificates of deposit with state-certified, qualified public depositories, as defined in F.S. § 280.02. Before investments are placed with an institution, a current financial statement and certification as an eligible public depository must be on file with the city. The city will limit the amount invested with any one institution to the federal FDIC insured limit to safeguard city funds.
- (6) The local Government Surplus Funds Trust Fund, or any intergovernmental investment pool authorized pursuant to the Florida Interlocal Cooperation Act of 1969, as provided in F.S. § 163.01.

(Ord. No. 98-03-01, § 1, 4-14-98)

Sec. 2-185. Investment officer.

The city's financial director, as the investment officer of the city is responsible for investment decisions and is directly responsible to the city manager. The day-to-day administration of the cash management program is handled by the financial director, and quarterly reports for submissions to the council shall include all investments by class or type, book value, income earned, and market value.

(Ord. No. 98-03-01, § 1, 4-14-98)

Sec. 2-186. Eligible depositories.

The following institutions are designated as eligible depositories for the city:

- (1) All state and national banks and/or state chartered savings and loans having principal offices in Florida insured by the Federal Deposit Insurance Corporation (FDIC), or its successor, and approved as eligible public fund depositories by the state.

(Ord. No. 98-03-01, § 1, 4-14-98)

Sec. 2-187. Local participation.

The city's intent is to support local financial institutions within its boundaries. Investments in institutions located outside the city boundaries will be made when competitive rates make this decision in the best interest of the city, or when investment timing requires investment alternatives and short-term yields not conveniently available from local financial institutions.

(Ord. No. 98-03-01, § 1, 4-14-98)

Sec. 2-188. Maturity schedule.

The financial director shall maintain a cash flow forecast to provide a guideline for supplementing cash flow with maturing investments to meet the cash flow needs of the city; therefore the maturity schedule should not exceed the cash needs of the city at any time. Investments which have a maturity schedule exceeding three years from the date of purchase shall be authorized by the city council.

(Ord. No. 98-03-01, § 1, 4-14-98)

Sec. 2-189. Internal controls.

The following internal controls and operational procedures will aid in preventing losses of city funds:

- (1) Bearer form securities shall not be purchased.
- (2) Promptly confirming telephone transactions in writing. All investment transactions will be supported by written confirmation, such as a confirmation ticket issued by the broker/dealer.
- (3) Documenting transactions. No withdrawal of securities, in whole or in part, shall be made from safekeeping, except by the authorized persons of the city, that being the city manager and the city clerk or in the absence of one, the mayor may sign. In the absence of both, the mayor and one council member may sign, with this procedure requiring the city council's approval. Securities transactions between a broker-dealer and the investment officer involving purchase or sale of securities by transfer of money or securities must be made on a "delivery vs. payment" basis, to ensure that the investment officer will have the security or money, as

appropriate, in hand at the conclusion of the transaction.

- (4) In addition, the city's independent auditors shall perform a review of all investment activities on an annual basis for submission to the council. The controls shall be designed to prevent loss of public funds from fraud, error, misrepresentation by another party, or imprudent actions by an employee or employees of the city.

(Ord. No. 98-03-01, § 1, 4-14-98)