

CITY OF LEXINGTON



INVESTMENT POLICY **(Adopted by City Council on 08/12/2019)**

City of Lexington Investment Policy

I. Governing Authority

Legality

The investment program shall be operated in conformance with federal, state and other legal requirements, including North Carolina General Statute 159-30.

II. Purpose

The purpose of this investment policy is to set forth the investment and operational guidelines for the management of the public funds of the City of Lexington. This policy is designed to ensure the prudent management of public funds, the availability of operating and capital funds when needed, and a competitive return on investments.

A copy of this policy will be provided to all investment broker/dealers and investment managers doing business with the City, and also will be provided to other interested parties upon request. Receipt of this policy, including confirmation that persons dealing directly with the City's account have reviewed it, will be received prior to any organization providing investment services to the City.

III. Scope

This policy applies to the investment of all City funds, excluding the investment of funds that may be held for the benefit of retirees in either an irrevocable LEOSSA Trust or an irrevocable OPEB Trust.

1. Pooling of Funds

Except for cash in certain restricted and special funds, the City will consolidate cash and reserve balances from all funds to maximize investment earnings and to increase efficiencies with regard to investment pricing, safekeeping and administration. Cash being pooled/invested does not include municipal debt proceeds.

Investment income will be allocated to the various funds based on their respective participation and in accordance with generally accepted accounting principles.

IV. General Objectives

The primary objectives of investment activities shall be safety, liquidity, and return:

1. Safety

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 risk and interest rate risk.

a. Credit Risk

The City will minimize credit risk, which is the risk of loss of all or part of the investment due to the failure of the security issuer or backer, by:

- Limiting investments to the types of securities authorized by North Carolina General Statute 159-30
- Pre-qualifying and conducting ongoing due diligence of the financial institutions and broker/dealers with which the City will do business in accordance with Section VI
- Diversifying the investment portfolio so that the impact of potential losses from any one type of security or from any one individual issuer will be minimized.

City of Lexington Investment Policy

b. Interest Rate Risk

The City will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by:

- Structuring the investment portfolio so that security maturities match cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity
- Investing operating funds primarily in shorter-term securities, North Carolina Capital Management Trust (NCCMT) Government and Term Portfolios, investment pools established by the State Treasurer, or similar investments and limiting individual security maturity as well as the average maturity of the portfolio in accordance with this policy (see Section IX).

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 concurrent with cash needs 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). Alternatively, a portion of the portfolio may be placed in money market mutual funds or local government investment pools, which offer same-day liquidity for short-term funds.

3. Return

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. 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 generally be held until maturity with the following exceptions:

- A security with declining credit may be sold early to minimize loss of principal;
- Unanticipated liquidity needs of the portfolio require that the security be sold;
- In the event of a credit risk or default by a specific issuer, the investment officer shall review and, if appropriate, proceed to liquidate securities with comparable credit risks.

V. Standards of Care

1. Prudence

The standard of prudence to be used by City investment officials shall be the “uniform prudent investor act” standard and shall be applied in the context of managing an overall portfolio. Investment officers acting in accordance with established 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 and the liquidity and the sale of securities are carried out in accordance with the terms of this policy.

2. 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. Investment officials shall disclose any material interests in financial institutions with which they conduct business, in accordance with applicable laws. They shall further disclose any personal financial/investment positions that could be related to the performance of the investment portfolio. This disclosure need not include normal banking or brokerage relationships that are at normal market rates and conditions available to the general public. Investment officials shall refrain from

City of Lexington Investment Policy

undertaking personal investment transactions with the same individual with whom business is conducted on behalf of the City.

3. Delegation of Authority

Authority to manage the investment program is granted to the Finance Director, hereinafter referred to as the investment officer and derived from North Carolina General Statute 159-25(a)(6). Responsibility for the operation of the investment program is hereby delegated to the investment officer, who shall act in accordance with established procedures and internal controls for the operation of the investment program consistent with this investment policy. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the investment officer. The investment officer may designate one or more members of the staff to assist in the performance of functions of cash management and investing. Such delegation will not relieve the investment officer of responsibility for all transactions and executions performed by the designated individuals. The investment officer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

VI. Authorized Financial Institutions, Depositories and Broker/Dealers

A list will be maintained of financial institutions and depositories authorized to provide investment services. In addition, a list will be maintained of approved security broker/dealers selected by creditworthiness and/or other factors, such as FINRA broker check. These may include “primary” dealers or regional dealers that qualify under Securities and Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule).

All financial institutions and broker/dealers who desire to become qualified for investment transactions with the City must supply the following as appropriate:

- Audited financial statements demonstrating compliance with state and federal capital adequacy guidelines.
- Proof of Financial Industry Regulatory Authority (FINRA) certifications (not applicable to Certificate of Deposit counterparties).
- Proof of state registration.
- Completed Broker/Dealer Questionnaire and Investment Trading Relationship Agreement (not applicable to Certificate of Deposit counterparties).
- Certification of having read and understood and agreeing to comply with the City’s investment policy.
- Evidence of adequate insurance coverage.

VII. Safekeeping and Custody

1. Delivery vs. Payment

All trades of marketable securities will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible custody account prior to the release of funds.

2. Safekeeping

Securities will be held by a third-party custodian selected by the City with all securities held in the City’s name.

3. Internal Controls

The investment officer shall establish a system of internal controls. The controls shall be designed to prevent the loss of public funds arising from fraud, employee error, misrepresentation by third parties, unanticipated changes in financial markets, or imprudent actions by employees and officer of the City.

**City of Lexington
Investment Policy**

VIII. Suitable and Authorized Investments

1. Investment Types

Investments may be made in any type of security authorized by North Carolina General Statute 159-30. The Finance Director may elect to further limit the City's investment security authority.

2. Collateralization

In accordance with North Carolina General Statute 159-31, the investment officer will require that sufficient collateral be pledged for public funds.

IX. Investment Diversification & Constraints

1. Diversification

It is the policy of the City to diversify its investment portfolio. To eliminate risk of loss resulting from the overconcentration of assets in a specific maturity, issuer, or class of securities, all cash and cash equivalent assets in all City funds shall be diversified by maturity, issuer, and security type. Diversification strategies shall be determined and revised periodically by the investment officer for all funds.

In establishing specific diversification strategies, the following general policies and constraints shall apply: Portfolio maturities shall be staggered to avoid undue concentration of assets in a specific maturity sector. Maturities selected shall provide for stability of income and reasonable liquidity.

The following diversification limitations shall be imposed on the portfolio:

- **Maturity:** No more than 50% of the portfolio may be invested beyond 2 years
- **Default Risk:** In order to avoid over concentration in securities from a specific issuer or business sector (except for securities of the U.S. Treasury, investments in the NCCMT Government and Term Portfolios, and investment pools established by the State Treasurer):
 - a) No more than 80% of the portfolio may be invested in government agency paper (AP)
 - b) No more than 40% of the portfolio may be placed with a single issuer of government agency paper (AP)
 - c) No more than 40% of the portfolio may be invested in commercial paper (CP)
 - d) No more than 20% of the portfolio may be placed with a single issuer of commercial paper (CP)
 - e) No more than 40% of the portfolio may be invested in qualified banker's acceptances
 - f) No more than 20% of the City's portfolio may be placed with a single financial institution (must be identified as public funds and collateralized under the Pooling Method of collateralization as described in 20 N.C. Admin. Code 7 .0104)
- **Liquidity Risk:** Because of inherent difficulties in accurately forecasting cash flow requirements, a portion of the portfolio must be continuously invested in readily available funds such as NCCMT Government and Term Portfolios, local government investment pools (LGIPs) established by the State Treasurer, money market funds or overnight repurchase agreements in order to ensure that appropriate liquidity is maintained in order to meet ongoing obligations.

2. Maximum Maturities

To the extent possible, the City shall attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the City will not directly invest in securities maturing more than three (3) years from the date of purchase or in accordance with state and local statutes and ordinances.

City of Lexington Investment Policy

Reserve funds and other funds with longer-term investment horizons may be invested in securities exceeding three (3) years, if the maturity of such investments is made to coincide as nearly as practicable with the expected use of funds.

3. Competitive Bids

The investment officer shall obtain competitive bids for investment instruments based on diversification, maturity and cash flow considerations and requirements.

X. Reporting

1. Methods

The investment officer shall prepare monthly investment reports for management purposes. These reports shall be reviewed by the Finance Director and will be made available for the City Manager, City Council and/or other parties as desired. The reports will include information on investment types, market values, maturity dates, and yield.

2. Performance Standards

The investment portfolio will be managed in accordance with the parameters specified within this policy. The portfolio should obtain a market average rate of return during a market/economic environment of stable interest rates.

3. Marking to Market

The market value of the portfolio shall be calculated and investments marked to market on a monthly basis. Reporting on the market value of the portfolio shall be disclosed semi-annually (or as requested) to City Council. This will ensure that review of the investment portfolio, in terms of value and price volatility, has been performed consistent as applicable with the GFOA Recommended Practice on “Mark-to-Market Practices for State and Local Government Investment Portfolios and Investment Pools.”

XI. Policy Considerations and Approval of Investment Policy

This policy shall be reviewed on a regular basis by the Finance Director. Proposed changes must be submitted by the Finance Officer for approval by City Council. The investment policy shall be formally approved and adopted by the City Council of the City of Lexington.

XII. Other Documentation

- Broker / Dealer Questionnaire
- Investment Trading Relationship Agreement