

## 103 INVESTMENT POLICY

It is the policy of TRWD that after allowing for the anticipated cash flow requirements of the District and giving due consideration to the safety and risk of investments, all available funds shall be invested in conformance with these legal and administrative guidelines, seeing to optimize interest earnings to the maximum extent possible.

Effective cash management is recognized as essential to good fiscal management. Investment interest is a source of revenue to TRWD funds. The District's investment portfolio shall be designed and managed in a manner which maximizes this revenue source, is responsive to public trust, and complies with legal requirements and limitations.

Investments shall be made with the primary objectives of:

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

**103.1 Purpose.** The purpose of this Investment Policy is to comply with Texas Water Code Chapter 49 and Texas Government Code Chapter 2256, the Public Funds Investment Act, which requires the governing body of a local governmental entity, such as TRWD, to adopt a written investment policy regarding the investment of its funds and funds under its control. The Investment Policy addresses the methods, procedures, and practices that must be exercised to ensure effective and judicious fiscal management of TRWD's funds.

**103.2 Scope.** This Investment Policy shall govern the investment of all financial assets of TRWD. These funds are accounted for in TRWD's Annual Financial Report and include:

- General Fund;
- Governmental Contingency Fund;
- Capital Projects Fund – TRV;
- Governmental Debt Service Fund;
- Revenue Fund;
- Interest and Redemption Fund;
- Enterprise Contingency Fund;
- Reserve Fund;

- Enterprise Construction Funds;
- Dallas - Revenue Fund;
- Dallas - Interest and Redemption Fund;
- Dallas - Reserve Fund;
- Dallas - Bond Funds; and,
- Any new fund created by the District, unless specifically exempted from this Investment Policy by law.

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

**103.3 Investment Objectives.** TRWD shall manage and invest its cash with four primary objectives, listed in order of priority: (1) safety; (2) liquidity; (3) public trust; and (4) yield, expressed as optimization of interest earnings. The safety of the principal invested always remains the primary objective. All investments shall be designed and managed in a manner responsive to the public trust and consistent with local, state, and federal law.

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

**103.3.1 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. The objective will be to mitigate credit and interest rate risk.

Credit Risk. TRWD will minimize credit risk, the risk of loss due to the failure of the issuer or backer of the investment, by:

- Limiting investments to the safest type of investments;
- Researching the financial institutions and broker/dealers with which TRWD will do business; and,
- Diversifying the investment portfolio so that potential losses on individual issuers will be minimized.

Interest Rate Risk. TRWD will minimize the risk that the interest earnings and the market value of investments in the portfolio will fall due to changes in general interest rates, by:

- Structuring the investment portfolio so that investments mature to meet cash requirements for ongoing operations, thereby avoiding the need to liquidate investments prior to maturity; and
- Diversifying maturities and staggering purchase dates to minimize the impact of market movements over time.

**103.3.2 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 investments mature concurrent with cash needs to meet anticipated demands. Because all possible cash demands cannot be anticipated, a portion of the portfolio will be invested in local government investment pools that offer same-day liquidity.

**103.3.3 Public Trust.** All participants in TRWD's investment process shall seek to act responsibly as custodians of the public trust. Investment officers shall avoid any cash management transaction that might impair public confidence in TRWD's ability to effectively manage the District's financial assets.

**103.3.4 Yield (Optimization of Interest Earnings).** The investment portfolio shall be designed with the objective of attaining a market rate of return sufficient to meet operating needs, 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.

#### **103.4 Responsibility and Control.**

**103.4.1 Delegation of Authority to Investment Officer(s).** In accordance with the Public Funds Investment Act and the Water Code, the Board of Directors may designate one or more officers or employees of TRWD to be Investment Officer(s) or may contract with a person to act as an Investment Officer. An Investment Officer is authorized to execute investment transactions on behalf of the District. No person may engage in an investment transaction or the management of District funds except as provided under the terms of this Investment Policy as approved by the Board of Directors. The investment authority granted to the investing officers is effective until rescinded by the Board of Directors.

**103.4.2 Quality and Capability of Investment Management.** All TRWD's designated investment officers and other investment personnel must receive all required training under Section 49.157 of the Water Code to ensure the quality and capability of investment management. The Board may designate approved training from an independent source for TRWD's investment officers and other investment personnel.

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

The internal controls shall address the following points:

- Avoidance of collusion;
- Separation of transaction authority;
- Custodial safekeeping;
- Clear delegation of authority to subordinate staff members; and,
- Written confirmation for investments and wire transfers.

The Chief Financial Officer shall establish a process for annual independent review by an external auditor, consistent with Sections 11.2 and 11.3 of the Board Governance Policies, to assure compliance with policies and procedures.

**103.4.4 Standard of Prudence.** The standard of prudence to be applied by the Investment Officer(s) shall be the "prudent investor" rule. Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

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

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

**103.4.5 Indemnification.** The Investment Officer(s), acting in accordance with written procedures and exercising due diligence, shall not be held personally responsible for a specific investment's credit risk or market price changes,

provided that these deviations are timely reported and the appropriate action is taken to control adverse developments.

**103.4.6 Ethics and Conflicts of Interest.** Investment Officers and employees involved in the investment process shall refrain from personal business activity that would conflict with the proper execution and management of the investment program, or that would impair their ability to make impartial decisions.

Investment Officers shall disclose any material interests in financial institutions with which they conduct business. They shall further disclose any personal financial/investment positions that could be related to the performance of the investment portfolio.

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

An investment officer has a personal business relationship with a business organization if:

- The investment officer owns 10 percent or more of the voting stock or shares of the business organization or owns \$5,000 or more of the fair market value of the business organization'
- Funds received by the investment officer from the business organization exceed 10 percent of the investment officer's gross income for the previous year; or
- The investment officer has acquired from the business organization during the previous year investments with a book value of \$2,500 or more for the personal account of the investment officer.

### **103.5 Suitable and Authorized Investments.**

**103.5.1 Portfolio Management.** TRWD currently has a "buy and hold" portfolio strategy. Maturity dates are matched with cash flow requirements and investments are purchased with the intent to be held until maturity. Investments may be liquidated prior to maturity, however, for the following reasons:

- An investment with declining credit may be liquidated early to minimize loss of principal.

- Cash flow needs of the District require that the investment be liquidated.

**103.5.2 Investments.** TRWD funds governed by this Investment Policy may be invested in the instruments described below, along with any other instruments authorized by the Public Funds Investment Act. Investment of District funds in any instrument or security not authorized for investment under the Act is prohibited. TRWD will not be required to liquidate an investment that becomes unauthorized subsequent to its purchase.

Authorized Investments: Authorized investments in which TRWD funds governed by this policy may be invested include:

- Obligations of the United States of America, its agencies, and instrumentalities.
- Certificates of Deposit issued by a bank organized under Texas law, the laws of another state, or federal law, that has its main office or a branch office in Texas, or by a savings and loan association or a savings bank organized under Texas law, the laws of another state, or federal law, that has its main office or a branch office in Texas and that is guaranteed or insured by the Federal Deposit Insurance or its successor or secured by obligations in a manner and amount provided by law for deposits of the District.
- Money Market Mutual funds that are (1) registered and regulated by the Securities and Exchange Commission; (2) have a dollar weighted average stated maturity of 90 days or less; (3) rated AAA by at least one nationally-recognized rating service, and (4) seek to maintain a net asset value of \$1.00 per share.
- Local government investment pools, which (1) meet the requirements of Texas Government Code § 2256.016; (2) are rated no lower than AAA or an equivalent rating by at least one nationally-recognized rating service; (3) seek to maintain a \$1.00 net asset value; and, (4) are authorized by resolution or ordinance adopted by the Board of Directors.
- Municipal bonds issued by a state or local municipality, which (1) meet the requirements of Section 2256.009 of the Public Funds Investment Act; and (2) are rated no lower than AAA or equivalent rating by at least one nationally-recognized rating service.

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

Investments Not Authorized. Investments including interest-only or principal-only strips of obligations with underlying mortgage-backed security collateral, collateralized mortgage obligations with an inverse floating interest rate or a maturity date of over ten years are strictly prohibited.

**103.5.3 Maximum Maturities.** The longer the maturity of investments, the greater their price volatility. It is, therefore, TRWD's policy to concentrate its investment portfolio in shorter-term securities to limit principal risk caused by changes in interest rates.

TRWD attempts to match its investments with anticipated cash flow requirements. Specific maturity limitations are discussed below with respect to each Fund's strategy.

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

- Limiting investments to avoid over-concentration in investments from a specific issuer or business sector (excluding U.S. Treasury securities and certificates of deposit that are fully insured and collateralized in accordance with state and federal law);
- Limiting investment in investments that have higher credit risks, such as commercial paper;
- Investing in investments with varying maturities; and,
- Continuously investing a portion of the portfolio in readily available funds such as local government investment pools or money market funds to ensure that appropriate liquidity is maintained to meet ongoing obligations.

## **103.6 Selection of Banks and Dealers**

**103.6.1 Depository.** At least every five years, the Finance and Audit Committee, along with TRWD staff, will review TRWD's Depository agreement. As part of this review, the Finance and Audit Committee will seek updated pricing and services offered to ensure alignment with TRWD's procedures and goals.

**103.6.2 Authorized Brokers/Dealers.** In consultation with the Finance and Audit Committee, TRWD shall, at least annually, review, revise and adopt a list of qualified brokers/dealers and financial institutions authorized to engage in

securities transactions with the District. Those firms that request to become qualified bidders for securities transactions will be required to provide a completed broker/dealer questionnaire that provides information regarding creditworthiness, experience, and reputation. Authorized firms may include primary dealers or regional dealers that qualify under Securities & Exchange Commission Rule 15C3-1, and qualified depositories. TRWD will provide a copy of this Investment Policy to all broker/dealers authorized to engage in securities transactions with the District. Investment pools must sign a certification acknowledging that the organization has received and reviewed TRWD's Investment Policy and that reasonable procedures and controls have been implemented to preclude investment transactions that are not authorized by this Investment Policy.

**103.6.3 Competitive Bids.** It is TRWD's policy to use competitive bidding for all individual security purchases and sales except for: (a) transactions with money market mutual funds and local government investment pools and (b) treasury and agency securities purchased at issue through an approved broker/dealer or financial institution.

**103.6.4 Delivery vs. Payment.** Securities shall be purchased using the delivery vs. payment method with the exception of investment pools and mutual funds. Funds will be released after notification that the purchased security has been received.

### **103.7 Safekeeping of Securities and Collateral**

**103.7.1 Safekeeping and Custodian Agreements.** TRWD shall contract with a bank or banks for the safekeeping of securities either owned by the District as part of its investment portfolio or held as collateral to secure demand or time deposits. Securities owned by TRWD shall be held in the District's name as evidenced by safekeeping receipts of the institution holding the securities.

Collateral for deposits will be held by a third-party custodian designated by the District and pledged to the District as evidenced by safekeeping receipts of the institution with which the collateral is deposited. Original safekeeping receipts shall be retained. Collateral may be held by the depository bank's trust department, a Federal Reserve Bank or branch of a Federal Reserve Bank, a Federal Home Loan Bank, or a third-party bank approved by the District.

**103.7.2 Collateral Policy.** Consistent with the requirements of Chapter 2257 of the Texas Government Code, the Public Funds Collateral Act, it is TRWD's policy to require full collateralization of all District funds on deposit with a depository bank, other than investments. In order to anticipate market changes and provide a level of security for all funds, the collateralization level will be 102% of market value



of principal and accrued interest on the deposits or investments less an amount insured by the FDIC. At its discretion, TRWD may require a higher level of collateralization for certain investment securities. Securities pledged as collateral shall be held by an independent third party with whom TRWD has a current custodial agreement. The agreements are to specify the acceptable investment securities for collateral, including provisions relating to possession of the collateral, the substitution or release of investment securities, ownership of securities, and the method of valuation of securities. A clearly marked evidence of ownership must be supplied to the District and retained.

Collateral shall be reviewed annually by TRWD's external auditors to assure that the market value of the pledged securities is adequate.

**103.7.3 Accepted Collateral.** The District shall accept only the following types of collateral:

- Obligations of the United States or its agencies and instrumentalities;
- Direct obligations of the State of Texas or its agencies and instrumentalities;
- Obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally-recognized rating firm not less than A or its equivalent with a remaining maturity of ten years or less;
- A surety bond issued by an insurance company rated as to investment quality by a nationally-recognized rating firm not less than A; and
- A letter of credit issued to the District by the Federal Home Loan Bank.

**103.7.4 Subject to Audit.** All collateral may be subject to inspection and audit by TRWD's external auditors.

## **103.8 Performance.**

**103.8.1 Performance Standards.** TRWD's investment portfolio will be managed in accordance with the parameters specified within this Investment Policy. The portfolio shall be designed with the objective of obtaining a rate of return through operating cycles, commensurate with the investment risk constraints and the cash flow requirements of the District.

**103.8.2 Performance Benchmark.** It is TRWD policy to purchase investments with maturity dates coinciding with cash flow needs. Through this

strategy, TRWD shall seek to optimize interest earnings utilizing allowable investments available on the market at that time. Market value will be calculated on a quarterly basis on all securities owned and compared to current book value.

### **103.9 Reporting.**

**103.9.1 Reporting Methods.** The Investment Officer(s) shall prepare an investment report on a quarterly basis that summarizes investment strategies employed in the most recent quarter and describes the portfolio in terms of investment securities and maturities and shall explain the total investment return for the quarter.

The quarterly investment report shall include a summary statement of investment activity prepared in compliance with generally-accepted accounting principles. This summary will be prepared in a manner that will allow TRWD to ascertain whether investment activities during the reporting period have conformed to the Investment Policy. The quarterly investment report will be provided to the Board of Directors. The report will include the following:

- A listing of individual securities held at the end of the reporting period.
- Unrealized gains or losses resulting from appreciation or depreciation by listing the beginning and ending book and market value of securities for the period.
- Additions and changes to the market value during the period.
- Listing of investments by maturity date.
- Fully-accrued interest for the reporting period.
- The percentage of the total portfolio that each type of investment represents.
- A statement of compliance of the District's investment portfolio with state law and this Investment Policy.

TRWD's external auditor will perform a formal annual review of the quarterly reports with the results reported to the Board of Directors as part of the yearly audit.

**103.9.2. Monitoring Market Value.** The market value of all securities in the portfolio will be determined on a quarterly basis. These values will be obtained from a reputable and independent source and disclosed quarterly in a written report provided to the Board of Directors.

The Investment Officer(s) shall monitor the credit ratings on securities that require minimum ratings. This may be accomplished through website research, or with the assistance of investment advisors, broker dealers, banks, or safekeeping agents. If any security falls below the minimum rating required by this Investment Policy, the Investment Officer(s) shall notify the General Manager of the loss of rating, conditions affecting the rating and possible loss of principal with liquidation options available.

## **103.10 Fund Strategies**

**103.10.1 Objectives.** Investments in all funds discussed below shall be made with the primary objectives of: (1) safety and preservation of principal; (2) liquidity; (3) diversification; and (4) optimization of interest earnings, as follows:

Safety and Preservation of Principal. TRWD maximizes safety and preservation of principal by limiting investments to the safest types of investments and researching the financial institutions and broker/dealers with which the District conducts business.

Liquidity. Liquidity needs are discussed below within each fund type.

Diversification. Within each of TRWD's funds, diversification is achieved by staggering both maturities and purchase dates to minimize the impact of market movements over time.

Optimization of Interest Earnings. Each fund's investment portfolio shall be designed to obtain a market rate of return sufficient to meet operating needs.

An explanation of each fund's specific purpose and primary strategy is listed below.

**103.10.2 General Fund.** The General Fund accounts for flood control, recreation, economic development, and general operations of the District. Funds available in the General Fund are used to pay the ongoing operational expenditures each fiscal year.

The primary strategy is to match the operational expenditures of the General Fund with tax revenues, investment interest, maturing investments, and other income sources, and invest any surplus fund balance to match future expenditure cash flow needs.

Maximum Maturity – 3 Years

**103.10.3 Governmental Contingency Fund.** This fund holds non-tax revenue for the Governmental Funds and can be used for Board-approved projects including but not limited to recreation and economic development.

All interest earnings from the Governmental Contingency Fund are reinvested in the Governmental Contingency Fund.

The primary strategy of the Governmental Contingency Fund is to purchase investments utilizing current coupon obligations to meet liquidity needs.

Maximum Maturity – 3 Years

**103.10.4 Capital Projects Fund.** This fund accounts for unexpended construction proceeds for Governmental Capital projects. Interest earnings from this fund are transferred to the Debt Service Fund to help pay the debt service on the governmental bonds; if no bonds are outstanding interest earnings will remain in the Capital Projects fund.

The primary strategy of this fund is to match maturing investments with anticipated project cash flow needs. Shorter-term obligations and Investment Pools are used to match any immediate liquidity needs that arise due to the estimation of the construction process and its related cash flows.

Maximum Maturity – 3 Years

**103.10.5 Governmental Debt Service Fund.** The Governmental Debt Service Fund accounts for the monies used to pay the debt service on outstanding governmental bonds. Interest earnings from the Capital Projects Funds are transferred to the Interest and Redemption Fund for debt service.

The primary strategy of this fund is to use investments with maturity dates on or before the debt service payment dates.

Maximum Maturity – 6 Months

**103.10.6 Revenue Funds.** The Revenue Funds account for the operation of TRWD's water supply and water sales functions. Income from water sales, interest earnings, and other income sources are used to pay the ongoing operational expenses each fiscal year. In addition, monies required to supplement the District's and Dallas's revenue bonds debt service are transferred to the District's and Dallas's Interest and Redemption Funds semi-annually (respectively).

The primary strategy is to keep all investments short-term in nature, allowing maturities to match the semi-annual outflows to the Interest and Redemption Fund and any operational expenses as they arise.

Maximum Maturity – 9 Months

**103.10.7 Enterprise Construction Funds –Bond Issue Funds.** These funds account for unexpended construction proceeds for the various Construction Funds projects. Interest earnings from these funds are transferred to the Interest and Redemption Fund (TRWD and Dallas respectively) to help pay the semi-annual debt service on the revenue bonds.

The primary strategy of these funds is to match maturing investments with anticipated construction cash flow needs. Shorter-term obligations and Investment Pools are used to match any immediate liquidity needs that arise due to the estimation of the construction process and its related cash flows.

Maximum Maturity – 3 Years

**103.10.8 Interest and Redemption Funds.** These funds account for the monies used to pay the semi-annual debt service on outstanding revenue bonds. Interest earnings from the Enterprise Construction Funds and the Reserve Funds are transferred to the Interest and Redemption Funds (for TRWD and Dallas respectively) prior to the semi-annual debt service dates. Any remaining funds needed are transferred from the respective Revenue Funds.

The primary strategy of these funds is to use investments with maturity dates on or before the semi-annual debt service payment date.

Maximum Maturity – 6 Months

**103.10.9 Reserve Funds.** These funds represent bond reserve funds associated with outstanding revenue bonded debt. The TRWD Reserve Fund is required to maintain a minimum market value equal to the maximum outstanding debt service payment in any given year. The Dallas Reserve Fund is required to maintain a minimum market value equal to the average annual outstanding debt service payment.. Interest earnings from these funds are transferred to the Interest and Redemption Fund (for TRWD and Dallas respectively) to help pay the semi-annual debt service on the revenue and contract revenue bonds.

The primary strategy of the Reserve Funds is maintaining adequate market value to meet the reserve requirement.

Maximum Maturity – Not to exceed the District's last maturing revenue bond.

**103.10.10 Enterprise Contingency Fund.** This fund is established by bond covenant and is to be used primarily for unexpected or extraordinary expenses of the water supply system for which other funds are not otherwise available. This fund can also be used to pay debt service when funds in the Interest and Redemption

Fund are insufficient for that purpose. The Enterprise Contingency Fund contains moneys received as buy-in premiums from additional water customers who purchased the right to buy water at the system rate. These buy-in premiums are kept in the Enterprise Contingency Fund at the request of the District's customer advisory board. All interest earnings from the Enterprise Contingency Fund are reinvested in the Enterprise Contingency Fund.

The primary strategy of the fund is to purchase investments, utilizing current coupon obligations to meet liquidity needs.

Maximum Maturity – 3 Years

**103.11 Investment Policy Adoption and Amendment.** TRWD's Board of Directors shall adopt this Investment Policy by a resolution of the Board of Directors. It is TRWD's intent to comply with state laws and regulations. Accordingly, this Investment Policy shall be subject to revisions consistent with changing laws, regulations, and needs of the District. The Board of Directors shall adopt a resolution stating that it has reviewed the policy and investment strategies annually, approving any changes or modifications.