HISTORIC
FRANKLIN
TENNESSEE

Investment Policy

Approved June 27, 2017

Law Dept. approved 08.02.17

Policy Statement

It is the policy of the City of Franklin to invest its funds in a manner which will provide for the safety of principal with a market rate investment return, while meeting daily cash flow requirements, and conforming to all state statutes governing the investment of funds under control of the City.

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1 Introduction

This Investment Policy ("Policy") defines the parameters to which funds are to be invested by the City of Franklin (City). This Policy is intended to be broad enough to allow designated investment staff to function properly within the parameters of responsibility and authority, yet specific enough to safeguard the investment assets adequately. This Policy applies to all activities related to the prudent investing of its financial assets.

2 Governing Authority

The City of Franklin's Investment Policy shall be operated in conformance with federal, state, and other legal requirements, which governs the investment of public funds by cities and towns.

3 Scope

This Policy applies to the investment of all funds of the City of Franklin, excluding the retirement funds. Retirement funds and proceeds from certain bond issues, as well as separate foundation or endowment assets, are covered by separate policies.

Except for cash in certain restricted and special finds, 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. Investment income will be allocated to the various funds based on their respective participation and in accordance with generally accepted accounting principles.

4 Objectives

All the City's investment activity will be conducted in a manner that emphasizes attainment of the following four (4) controlling objectives:

- **Safety:** Safety of principal is the most 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 risk and interest rate risk.

  - *Credit Risk:* The City will minimize credit risk, which is the risk of loss due to the failure of the security issuer or backer, by:

    Limiting investments to the types of securities listed in this Policy;

    Pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisers with which the City will do business;

    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.

  - *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 securities mature to meet cash requirements for ongoing

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operations, thereby avoiding the need to sell securities on the open market prior to maturity;

Investing operating funds primarily in shorter-term securities, money market mutual funds, or similar investment pools and limiting the average maturity of the portfolio in accordance with this policy.

- **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, bank repurchase agreements, or local government investment pools, which offer same-day liquidity for short-term funds.

- **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 of investments is 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;
  - A security swap would improve the quality, yield, or target duration in the portfolio; Liquidity needs of the portfolio require that the security be sold.

- **Local Considerations:** The City of Franklin seeks to promote local economic development through various programs and activities. Included is a program of rewarding local financial institutions that increase their commitments to private economic growth and local housing investment.

  The City may accept a proposal from an eligible institution that provides for a reduced rate of interest provided that such institution documents the use of deposited funds for community development projects. All terms and relationships will be fully disclosed prior to purchase, will be reported to the Budget and Finance Committee on a regular basis, and should be consistent with state or local law.

5 Standards of Care

- **Delegation of Authority:**

  Governing Body: The Board of Mayor and Aldermen will retain ultimate fiduciary responsibility for the portfolios and have the authority to direct the management of the investment program.

  Chief Financial Officer: Authority to manage the investment program is granted to the Chief Financial officer, hereinafter referred to as investment officer. The investment officer shall establish written procedures for the operation of the investment program, consistent with this investment policy. The investment officer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate all activities of the program.

- **Prudence:**

  The standard of prudence to be used in the context of managing the overall portfolio is the prudent person rule which states:

  > *Investments will 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 in regard to speculation but in regard to the permanent disposition of the funds considering the probable income as well as the probable safety of the capital.*

- **Ethics and Conflict of Interest:**

  City of Franklin employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution and management of the investment program or which could impair their ability to make impartial investment decisions. They shall disclose any material financial interests and any large personal financial / investment positions that could be related to the performance of the City's portfolio.

6 Authorized Counterparty Institutions

- **Broker/Dealers:** The Investment Officer shall maintain and review annually a list of all authorized broker/dealers that are approved to transact with the City for investment purposes.

  The Investment Officer or designee may utilize the investment advisor's approved broker/dealer list in lieu of the City's own approved list. The advisor must submit the approved list to the City annually and provide updates throughout the year as they occur. The advisor must maintain documentation of appropriate license, professional credentials and financial statements of broker/dealers on the list.

  Annual review must include the following documentation:
  - Proof of FINRA Registration
  - Proof of State Registration
  - Financial Review
  - Broker Check for Violations

- **Financial Institution Depositories:** All financial institutions who desire to become depositories must meet the statute requirements to maintain deposits in the State of Tennessee and must provide the following:

  - Audited financial statements demonstrating compliance with state and federal capital adequacy guidelines
  - Proof of state registration
  - Evidence of adequate insurance coverage

- **Investment Advisers:** The City may engage the services of an external investment adviser, with the approval of the Board of Mayor & Aldermen, to assist with the management of its investment portfolio in a manner that is consistent with the City's controlling objectives. Such advisers may be granted the authority to purchase and sell investments in accordance with this Investment Policy, and the adviser may only provide non-discretionary management services, which requires prior authorization from the City on all transactions.

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Such Advisers must be registered under the Investment Advisers Act of 1940, with the Securities and Exchange Commission, and their performance will be periodically reviewed by City management. Investment advisory services will be acquired through a competitive bidding process.

The investment adviser's responsibilities include the following:

- Determine the targeted risk profile and allocation among allowable investments
- Determine the number, type and structure of investments within the confines set forth by and reflected in this Policy.

7 Safekeeping, Custody, and Controls

- **Delivery vs. Payment:**

  All trades of marketable securities will be executed (cleared and settled) on a delivery vs. payment (DVP) basis to ensure that securities are deposited in the City's safekeeping institution prior to the release of funds.

- **Third Party Safekeeping:**

The investment officer shall designate all safekeeping arrangements and an agreement of the terms shall be executed in writing. The third-party custodian shall be required to provide a statement to the City listing, at a minimum, each specific security, book yield, description, maturity date, market value, par value, purchase date, and CUSIP number. All securities pledged to the City for certificates of deposit or demand deposits shall be held in a segregated account at the issuing financial institution.

- **Collateralization:**

In accordance with Tennessee Code Annotated, full collateralization will be required on all demand deposit accounts, including checking accounts, negotiable certificates of deposit, and non-negotiable certificates of deposit, except when the institution issuing the certificate of deposit belongs to the Tennessee Bank Collateral Pool.

- **Internal Controls:**

  Management will establish and maintain internal controls designed to provide reasonable assurance that the assets of the City are protected from loss, theft or misuse. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived.

8 Suitable and Authorized Investments

All investments of the City are to be permissible as required by the Tennessee Code Annotated.

This policy recognizes S&P, Moody's and Fitch as the major Nationally Recognized Statistical Ratings Organizations (NRSRO).

In the case of split ratings, where the major NRSROs issue different ratings, at least two must have the AA- or its equivalent.

Minimum credit ratings and percentage limitations apply to the time of purchase.

Idle Funds of the City:

1) **U. S. Treasury Obligations:** Bonds, notes or treasury bills of the United States;

2) **GSE – Primary Agency Obligations:** Government Sponsored Enterprises (GSEs) – Non-convertible debt securities of the following federal government: Federal Home Loan Banks (FHLB); Federal National Mortgage Association (FNMA), the Federal Farm Credit Bureau (FFCB), and the Federal Home Loan Mortgage Corporation (FHLMC).

3) **GSE – Secondary Agency Obligations:** Any other obligations not listed as primary agency, that are guaranteed as to principal and interest by the United States or any of its agencies. They include, but are not limited to: Private Export Funding Corporation (PEFCO), Tennessee Valley Authority (TVA), Financing Corporation (FICO) and Federal Agricultural Mortgage Corporation, (Farmer Mac). Securities must be rated.

4) **Certificates of deposit and other evidences of deposit at state and federally chartered banks and savings and loan associations:** Notwithstanding any other public or private act to the contrary, all investments made shall be secured by collateral in the same manner and under the same conditions as state deposits, or as provided in a collateral pool created; This includes: Negotiable and Non-Negotiable CD's, CDAR's and ICS money market offerings of state and federal banks.

5) **Repurchase Agreements:** Obligations of the United States or its agencies under a repurchase agreement for a shorter time than the maturity date of the security itself if the market value of the security itself is more than the amount of funds invested; provided, that municipalities may invest in repurchase agreements only if the comptroller of the treasury or the comptroller's designee approves repurchase agreements as an authorized investment, and if such investments are made in accordance with procedures established by the state funding board.

6) **Local Government Investment Pool:** Part of the State Pooled Investment Fund administered by the Tennessee Department of Treasury.

7) **Bankers' Acceptances:** Prime bankers' acceptances that are eligible for purchase by the federal reserve.

8) **Commercial Paper:** Prime commercial paper that is rated at least A 1 or equivalent by at least two (2) nationally recognized rating services.

9) **Municipal Debt Obligations of the City:** The City's own bonds or notes issued in accordance with title 9, chapter 21.

10) **Investment in the instruments or any type of investment authorized pursuant to a municipality's charter that is of a type that is not included in this part shall require the following:**

    a. The municipality's Board of Mayor and Aldermen must authorize the investment by ordinance; and
    b. The Board of Mayor and Aldermen must adopt a written enforceable investment policy by ordinance to govern the use of investments, with the policies being no less restrictive than those established by the state funding board to govern state investments in these types of instruments.

Investment in instruments not allowable in the section are prohibited until the legislative body has adopted written policies to govern the use of the investments or an ordinance has been passed to authorize the investment

Bond Proceeds Only:

Proceeds of bonds, notes and other obligations issued by municipalities, reserves held in connection therewith and the investment income therefrom, may be invested in obligations that:

1) **Ratings:** Are rated in either of the two (2) highest rated categories by a nationally recognized rating agency of such obligation (AA- S&P, Aa3, Moody's or AA- by Moody's.

2) **US Treasury or Agency Bonds** that are direct general obligations of a state of the United States.

3) **Municipal Bonds:** a political subdivision or instrumentality thereof, having general taxing powers; and

4) **Maturity:** Have a final maturity on the date of investment of not to exceed forty-eight (48) months or that may be tendered by the holder to the issuer thereof, or an agent of the issuer, at not less than forty-eight-month interval.

9 Investing Parameters

Diversification:

The City will diversify the investment of all funds in accordance with the following table:

Table of Constraints on the Portfolio

Issue Type	Maximum % Holdings	Maximum % per Issuer	Collateral Required	Ratings S&P	Ratings Moody's	Ratings Fitch
US Treasury Obligations	100%	None	N/A	N/A	N/A	N/A
US Agency Primary Securities FHLB, FNMA, FHLMC, FFCB	100%	35%	N/A	N/A	N/A	N/A
US Agency Secondary Securities FICO, FARMER MAC etc. must be rated	10%	5%	N/A	AA-	Aa3	AA-
Certificates of Depost and other evidences of deposit, including time deposits, CDARS and ICS funds	50%	50%	Fully Collateralized or other evidences of deposit under section 6-56-106 (a)(4)	N/A	N/A	N/A
Repurchase Agreements	10%	None	Fully Collateralized US Treasury or Agency Securities	N/A	N/A	N/A
Local Government Investment pool	100%	None	Participant	N/A	N/A	N/A
Bankers Acceptance	10%	5%	N/A	A1	P1	F1
Commercial Paper (must be rated by two rating agencies and under 90 days)	20%	5%	N/A	A1	P1	F1
City of Franklin Notes or Bonds	10%	N/A	N/A	N/A	N/A	N/A

10 Maturity Constraint

Total Portfolio Maturity Constraints:

Maturity Constraints	Minimum % of Total Portfolio
Under 30 days	10%
Under 2 years	50%
Under 4 years	100%
Maturity Constraints	**Maximum of Total Portfolio in Years**
Weighted Average Maturity	2.00
Security Structure Constraint	**Maximum % of Total Portfolio**
Callable Agency Securities	25%

11 Performance Measurement and Reporting

- **Performance Reporting:**

  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 over interest rate cycles. A market benchmark shall be established for the investment component of the portfolio and a comparison of the benchmark risk and return characteristics will be made to the investment portfolio.

  The City's cash management portfolio shall be designed with the objective of regularly meeting or exceeding a performance benchmark, such as the average return on three-month U.S. Treasury bills, the state investment pool, or the average rate on Fed funds, whichever is higher. These indices are considered benchmarks for lower risk investment transactions and therefore comprise a minimum standard for the portfolio's rate of return. The investment program shall seek to augment returns above this threshold, consistent with risk limitations identified herein and prudent investment principles

- **Reporting:**

  The Investment Officer shall prepare an investment report at least quarterly, including a management summary that provides an analysis of the status of the current investment portfolio and the individual transactions executed over the last quarter. This management summary will be prepared in a manner which will allow the City to ascertain whether investment activities during the reporting period have confirmed to the investment policy. The report should be provided to the City Administrator and to the Budget & Finance Committee. The report will include the following:

  a. An asset listing of individual securities showing par value, cost and accurate and complete market value of each security, type of investment, issuer, and interest rate;

b. Average maturity of the portfolio and modified duration of the portfolio;
c. Maturity distribution of the portfolio;
d. Average portfolio credit quality;
e. Time-weighted total rate of return for the portfolio for the prior one month, three months, twelve months, year-to-date, and since inception compared to the Benchmark Index returns for the same periods;
f. Average weighted yield to maturity of the portfolio on investments as compared to applicable benchmarks; and
g. Distribution by type of investment.

12 Policy Adoption

This Investment Policy is formally approved and adopted by the Board of Mayor & Aldermen.

CITY OF FRANKLIN:

06/27/17

Dr. Ken Moore, Mayor — Date

ATTEST:

Eric S. Stuckey

06/27/17

Eric S. Stuckey, City Administrator — Date

Approved as to form:

Shauna R. Billingsley

Shauna R. Billingsley, City Attorney

GLOSSARY OF TERMS

- **Agency Securities:** Government sponsored enterprises of the US Government.
- **Bond:** An interest-bearing security issued by a corporation, government, governmental agency, or other body. It is a form of debt with an interest rate, maturity, and face value, and specific assets sometimes secure it. Most bonds have a maturity of greater than one year and generally pay interest semiannually. *See* Debenture.
- **Broker:** An intermediary who brings buyers and sellers together and handles their orders, generally charging a commission for this service. In contrast to a principal or a dealer, the broker does not own or take a position in securities.
- **Collateral:** Securities or other property that a borrower pledges as security for the repayment of a loan. Also refers to securities pledged by a bank to secure deposits of public monies.
- **Commercial Paper:** Short-term, unsecured, negotiable promissory notes issued by corporations.
- **Current Maturity:** The amount of time left until an obligation matures. For example, a one- year bill issued nine months ago has a current maturity of three months.
- **CUSIP:** A CUSIP number identifies securities. CUSIP stands for Committee on Uniform Security Identification Procedures, which was established to develop a uniform method of identifying municipal, U.S. government, and corporate securities.
- **Dealer:** An individual or firm that ordinarily acts as a principal in security transactions. Typically, dealers buy for their own account and sell to a customer from their inventory.
- **Delivery:** Either of two methods of delivering securities: delivery vs. payment and delivery vs. receipt (also called "free"). Delivery vs. payment is delivery of securities with an exchange of money for the securities.
- **Duration:** A measure used to calculate the price sensitivity of a bond or portfolio of bonds to changes in interest rates. This equals the sum of the present value of future cash flows.
- **General Obligation Bonds (GOs):** Bonds secured by the pledge of the municipal issuer's full faith and credit, which usually includes unlimited taxing power.
- **Government Bonds:** Securities issued by the federal government; they are obligations of the U.S. Treasury; also known as "governments."
- **Investment Securities:** Securities purchased for an investment portfolio, as opposed to those purchased for resale to customers.
- **Liquidity:** The ease at which a security can be bought or sold (converted to cash) in the market. A large number of buyers and sellers and a high volume of trading activity are important components of liquidity.
- **Mark to Market**: Adjustment of an account or portfolio to reflect actual market price rather than book price, purchase price or some other valuation.
- **Prudent Person Rule:** A long-standing common-law rule that requires a trustee who is investing for another to behave in the same way as a prudent individual of reasonable discretion and intelligence who is seeking a reasonable income and preservation of capital.
- **Treasury Bill (T-Bill):** An obligation of the U.S. government with a maturity of one year or less. T-bills bear no interest but are sold at a discount.
- **Treasury Bonds and Notes:** Obligations of the U.S. government that bear interest. Notes have maturities of one to ten years; bonds have longer maturities.
- **Yield:** The annual rate of return on an investment, expressed as a percentage of the investment.
- **Yield to Maturity:** The average annual yield on a security, assuming it is held to maturity; equals to the rate at which all principal and interest payments would be discounted to produce a present value equal to the purchase price of the bond.

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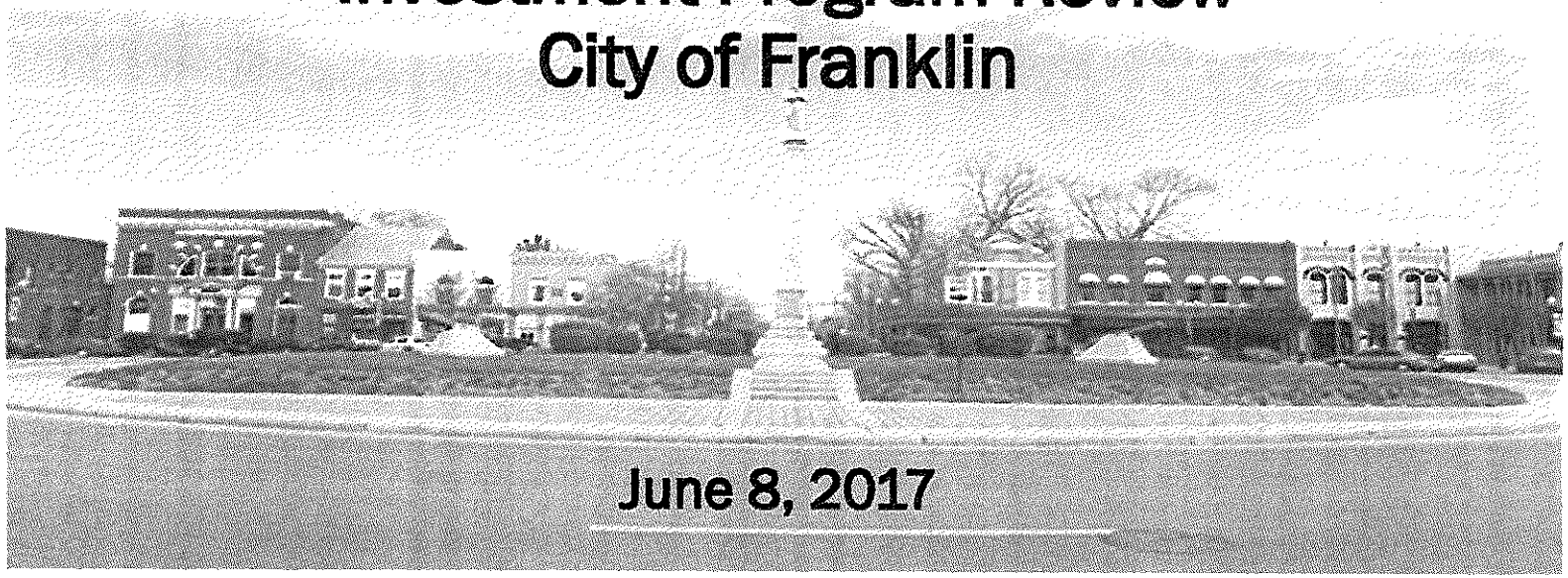
GOVERNMENT PORTFOLIO ADVISORS

Investment Program Review
City of Franklin



June 8, 2017

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