



INVESTMENT POLICY FOR THE CITY OF SEDONA

I. Purpose

The purpose of this policy is to guide the investment of funds for the City of Sedona, Arizona (hereinafter “the City”). This policy will update and replace the City’s Investment Policy adopted on November 22, 1998. The investment environment has changed significantly since 1998 and this current policy brings the City’s investment approach up to date while still maintaining the primary objectives of safety of principal, liquidity and yield, in priority order.

Therefore, it is the investment policy of the City, the City Manager and Financial Services Director to maintain the safety of principal, maintain liquidity in order to meet the cash flow needs of the City and provide competitive investment returns as identified below. The Financial Services Director will strive to invest with the judgment and care that a prudent individual would exercise with his or her own affairs.

II. Governing Authority

The investment program of the City shall operate in conformance with Federal, State and other legal requirements, primarily outlined in A.R.S. § 35-323.

III. Approval of the Investment Policy

The investment policy shall be formally approved and adopted by the City Council and reviewed annually by the City Manager and Financial Services Director.

IV. Scope

- The City will consolidate cash balances from all funds in order to maximize investment earnings and to increase efficiencies with regard to investment management pricing, safekeeping costs and administration costs, except for cash in certain restricted and/or specials funds, which may be exempted from this policy.
- Investment income will be allocated to the various funds based on their respective participation and in accordance with generally accepted accounting principles.

- The Financial Services Director shall follow A.R.S. § 35-323. Investments controlled by Internal Revenue Service's (IRS) Regulations, such as bond proceeds will be deposited into a separate account and invested in accordance with IRS guidelines.

V. Investment Policy Objectives

The primary investment objectives of the City in order of priority are:

- Safety
- Liquidity
- Optimal yield

These objectives are defined below:

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 prudently mitigate credit risk and interest rate risk. It is understood by the City that no investment is completely free of risk.

A. Credit Risk

The City will seek to mitigate credit risk, which is defined as the risk of loss due to the failure of the security issuer or backer. Mitigating credit risk is to be accomplished by:

- Limiting investments in the portfolio to the asset classes designated as acceptable in A.R.S. §35-323. When possible, analysis of the credit worthiness of all individual debt issuers held in the portfolio should be conducted on an annual basis in an effort to guard against investing in weak or deteriorating credit situations;
- Diversifying the investment portfolio so that the impact of potential losses from any one individual issuer held in the portfolio will be limited. Specific diversification parameters will be noted in Section VIII. Authorized Investments;
- Utilizing external research and advice regarding the current global economic condition and its impact on the outlook for domestic corporate credit quality.

B. Interest Rate Risk

The City will seek to mitigate interest rate risk, which is defined as the risk that the market value of securities held in the portfolio will decline due to increases in market interest rates subsequent to their purchase. This mitigation will be accomplished by:

- Structuring the investment portfolio so that securities mature concurrent with the anticipated cash requirements for ongoing operations, thereby avoiding, as much as possible, the need to sell securities into an adverse market environment prior to maturity;
- Investing funds primarily in shorter-term securities or similar investment pools and limiting the average maturity of the portfolio in accordance with the needs of the City;
- Utilizing external research and advice regarding the current interest rate outlook and global economic condition to optimize portfolio duration strategy.

Liquidity - The investment portfolio shall remain sufficiently liquid to meet anticipated cash flow requirements. This is to be accomplished by structuring the portfolio so that securities mature concurrent with anticipated cash flow needs (static liquidity). Furthermore, because all possible cash demands cannot be anticipated, the portfolio should consist of securities for which there exist active secondary markets (dynamic liquidity).

Optimal Yield - Return on investment is of lesser importance compared to the safety and liquidity objectives described above. The investment portfolio shall be designed to optimize the yield the City obtains from the portfolio taking into account the criteria of the investment policy, the dynamic liquidity needs of the City and the current interest rate outlook/economic condition.

VI. Investment Management Authority

Authority to either manage internally or to delegate the management of the investment portfolio of the City to an external manager is granted to the City Manager and his/her designee. If authority to manage all or a part of the investment portfolio of the City is delegated to an external manager, the City Manager and his/her designee shall be responsible for:

- Periodic investment portfolio reporting;
- Evaluating the performance of the externally managed portfolio;
- Confirming compliance with the City's investment policy;
- Developing investment strategies with the external manager and periodically reviewing the strategy to ensure it is consistent with the City's goals and values.

VII. Brokers/Dealers

When the City is investing directly with Brokers/Dealers, investment transactions shall be conducted only with financial institutions that are licensed, as may be required by

law, to do business in Arizona. Primary government securities dealers or broker-dealers, engaged in the business of selling government securities, shall be registered in compliance with section 15 or 15C of the Securities Exchange Act of 1934 and registered pursuant to A.R.S. §§44-3101-3159, as amended. It shall be the responsibility of the financial institutions and brokers/dealers to provide the following:

- Audited, most recent financial statements;
- Proof of Financial Industry Regulatory Authority certification;
- Proof of state registration (as needed);
- A signed letter acknowledging that they have read and agree to abide by the City's Investment Policy.

VIII. Authorized Investments

As of adoption of this Investment Policy A.R.S. §35-323 defines the acceptable classes available for Cities to invest in as follows:

1. Certificates of deposit in eligible depositories.
2. Deposits in one or more federally insured banks or savings and loan associations placed in accordance with the procedures prescribed in §35-323.01.
3. Interest bearing savings accounts in banks and savings and loan institutions doing business in this state whose accounts are insured by federal deposit insurance for their industry, but only if deposits in excess of the insured amount are secured by the eligible depository to the same extent and in the same manner as required under this article.
4. Repurchase agreements with a maximum maturity of one hundred eighty days.
5. The pooled investment funds established by the state treasurer pursuant to §35-326.
6. Obligations issued or guaranteed by the United States or any of the senior debt of its agencies, sponsored agencies, corporations, sponsored corporations or instrumentalities.
7. Bonds, notes or other evidences of indebtedness of this state or any of its counties, incorporated cities or towns, school districts or special taxing districts, including registered warrants that shall bear interest pursuant to A.R.S. §11-635.
8. Bonds, notes or evidences of indebtedness of any county, municipal district, municipal utility or special taxing district of any state that are payable from revenues, earnings or a special tax specifically pledged for the payment of the

principal and interest on the obligations, and for the payment of which a lawful sinking fund or reserve fund has been established and is being maintained, but only if no default in payment on principal or interest on the obligations to be purchased has occurred within five years of the date of investment, or, if such obligations were issued less than five years before the date of investment, no default in payment of principal or interest has occurred on the obligations to be purchased nor any other obligations of the issuer within five years of the investment.

9. Bonds, notes or evidences of indebtedness issued by any county improvement district or municipal improvement district of any state to finance local improvements authorized by law, if the principal and interest of the obligations are payable from assessments on real property within the improvement district. An investment shall not be made if:

(a) The face value of all such obligations, and similar obligations outstanding, exceeds fifty per cent of the market value of the real property, and if improvements on which the bonds or the assessments for the payment of principal and interest on the bonds are liens inferior only to the liens for general ad valorem taxes.

(b) A default in payment of principal or interest on the obligations to be purchased has occurred within five years of the date of investment, or, if the obligations were issued less than five years before the date of investment, a default in the payment of principal or interest has occurred on the obligations to be purchased or on any other obligation of the issuer within five years of the investment.

10. Commercial paper of prime quality that is rated within the top two ratings by a nationally recognized rating agency. All commercial paper must be issued by corporations organized and doing business in the United States.

11. Bonds, debentures, notes or other evidences of indebtedness that are denominated in United States dollars and that carry at a minimum an "A" or better rating, at the time of purchase, from at least two nationally recognized rating agencies.

12. Negotiable or brokered certificates of deposit issued by a nationally or state chartered bank or savings and loan association.

13. Securities of or any other interests in any open-end or closed-end management type investment company or investment trust, including exchange traded funds whose underlying investments are invested in securities allowed by state law, registered under the investment company act of 1940 (54 Stat. 789; 15 United States Code §§ 80a-1 through 80a-64), as amended.

All other investments are prohibited. The City may take a more conservative approach to its investments and restrict or prohibit certain allowed investments listed above.

Benchmark

The performance of an actively managed portfolio on behalf of the City will be expected to at least match the performance of the Arizona Local Government Investment Pool (LGIP) 5.

Concentration and Diversification

At the time of purchase a maximum of 5% of the market value of the portfolio may be invested in debt issued by any single entity. Debt backed by the United State Treasury or U.S. Government Sponsored Enterprises are exempt from this concentration criterion.

Safekeeping and Custody

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 financial institution prior to the release of funds.

Safekeeping – Securities will be held by a custodian selected by the City and evidenced by custodial reports. Securities will be registered in the name of the City of Sedona. The safekeeping institution shall provide a copy of their most recent report on internal controls (Statement of Auditing Standards No. 70, or SAS 70).

IX. Reporting

The Financial Services Director or his/her designee shall produce an investment report, at least quarterly, that is made available to the City Manager and the City Council. The purpose of the report is to enable the City to ascertain that the investment activities during the reporting period conform to the investment policy. The report should include:

- A list of individual securities held at the end of the reporting period;
- Realized and unrealized gains or losses in the portfolio;
- The duration of each security held and the portfolio as a whole;
- The maturity date of each security;
- The book value and fair market value of each security;
- The percent and value that each investment class represents;
- The coupon or periodic interest rate of each security held in the portfolio;
- A summary of the portfolio transactions, including fees incurred for external management and custody services.

X. Ethics and Conflicts of Interest

City officers and employees involved in the investment process shall refrain from personal business activities that could conflict with the proper execution and management of the investment program. City officers and employees shall refrain from undertaking personal investment transactions with the same individual(s) with which business is conducted on behalf of the City.

XI. Policy Considerations

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.

Any deviation from the preceding policy shall require the prior specific written authority of the City Council.

Approved this 11th day of August, 2015, by the Mayor and City Council of Sedona, Arizona.