

TOWN OF HERNDON, VIRGINIA INVESTMENT AND PORTFOLIO POLICY

SCOPE

This investment policy applies to the investment activities of the Town of Herndon, Virginia (Town). All financial assets of its funds, including the General Fund, the Water and Sewer Fund, the Chestnut Grove Cemetery Fund, the Golf Course Fund, the Downtown Parking Enterprise Fund, the Capital Projects Fund, and the Information Systems Improvement Fund, and other funds that may be created from time to time, with the exclusion of the Supplemental Retirement Plan for Police Employees, shall be administered in accordance with the provisions of these policies.

OBJECTIVES

Safety of principal is the foremost objective of the Town. Each investment transaction shall seek to first ensure that capital losses are avoided, whether they are from securities default or erosion of market value.

The Town's cash management portfolio shall be designed with the objective of regularly exceeding the average return on three-month U.S. Treasury bills, or the average rate on Federal funds, whichever is higher. These indices are considered benchmarks for riskless 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 here and prudent investment principles.

The Town's outside investment managers are encouraged to represent the Town's best interests in seeking to remove constraints to the efficient investment of its funds.

All participants in the investment process shall seek to act responsibly as custodians of the public trust. Investment officials shall avoid any transaction that might impair public confidence in the Town's ability to govern effectively.

INVESTMENT AND AUDITING OVERSIGHT COMMITTEE

There shall be a combined investment and auditing oversight committee composed of two members of Town Council, two members of Town management and two members of the public. The Town Council will appoint the two Council members at a public meeting and assign one of the two to be chair of the committee. The Town Manager will appoint the Director of Finance and the remaining three members to the committee. Members of the committee shall meet periodically to review general investment strategies and monitor results; to discuss internal controls and meet with the Town's independent certified public accounts; and to receive the Town's comprehensive annual financial report and management letter comments as part of the annual audit of the Town's financial records. The committee shall establish its own rules and procedures.

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DELEGATION OF AUTHORITY

The Town Manager delegates management responsibility for the investment program to the Director of Finance (Director) who, after consultation with the Town Manager and subsequent approval by the Town Council, shall establish written procedures for the operation of the investment program, consistent with this investment policy. These procedures shall include explicit delegation of authority to persons responsible for investment transactions. No person may engage in an investment transaction for the Town except as provided under the terms of this policy and the procedures established by the Director. The Director shall be responsible for the transactions undertaken and shall establish a system of internal controls to regulate the activities of subordinate officials.

PRUDENCE

The standard of prudence to be used by investment officials shall be the "prudent person" standard and shall be applied in the context of managing an overall portfolio. The Town shall relieve investment officers acting in accordance with law and written procedures and exercising due diligence of personal responsibility for credit risk or market price changes, provided deviations from expectations are reported to the Town Manager within two weeks of discovering such deviations and appropriate action is taken to control adverse developments.

ETHICS AND CONFLICTS OF INTEREST

Officers and employees involved in the investment process shall refrain from any personal business activity that could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions. Consistent with the State and Local Government Conflict of Interest Act (Sec. 2.2-3100 thru 2.2-3127 Code of Virginia), employees and investment officials shall disclose or otherwise take appropriate action with respect to any personal interest in any financial institution transaction or contract related to Town investments. Further, such employees and investment officials shall file a Statement of Economic Interest with the Town Clerk by January 15 of each calendar year, as described in Sec. 2.2-3115 Code of Virginia. Employees and officers shall subordinate their personal investment transactions to those of the Town, particularly with regard to the timing of purchases and sales.

INTERNAL CONTROLS

The Finance Director shall establish a system of internal controls, which shall be documented in writing. The internal control structure shall be designed to minimize or prevent loss of public funds arising from fraud, employee error, misrepresentation by third parties, unanticipated changes in financial markets, or imprudent actions by employees and officers of the Town.

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REPORTING: INTERIM AND ANNUAL

The Finance Director shall submit to the Town Manager a quarterly investment report that summarizes the status of the current investment portfolio and transactions made over the last quarter. The report will describe the portfolio in terms of investment securities, maturities, interest rates and other features. The report will explain the year-to-date total investment return and compare the return with budgetary expectations. The report will include an appendix that discloses all transactions during the reporting period. If warranted, the report will indicate any areas of policy concern and suggested or planned revision of investment strategies. Within 180 days after the end of the fiscal year, the Finance Director shall present to the Town Manager an annual report on the investment program and investment activity. The report shall be based on the audited numbers of the most recently concluded fiscal year. The annual report will include 12-month comparisons on return and, if warranted, suggest policies and improvements that could be made in the investment program. Information contained in the report will be sufficiently detailed so as to permit an independent evaluation of the performance of the investment program.

INSTRUMENTS

As a unit of local government in the Commonwealth of Virginia, the Town is governed by the Virginia Security for Public Deposits Act, 2.2-4400 through 2.2-4411 and the Investment of Public Funds as described in Sec. 2.2-4500 through 2.2-4517 of the Code of Virginia. The following securities may be purchased for the Town's investment portfolio:

- a) Bonds, notes and other evidences of indebtedness of the Commonwealth;
- b) Bonds, notes and other direct obligations of the United States and securities unconditionally guaranteed as to the payment of principal and interest by the United States or any agency thereof;
- c) Certificates of deposit and time deposits of Virginia banks and savings and loan institutions federally insured to the maximum extent possible and/or collateralized up to 100% of the amount of the deposit in excess of federal insurance coverage;
- d) Banker's Acceptances with major U.S. money center banks rated B/C or better in the Thompson Bank Watch;
- e) Local Government Investment Pool operated by the Treasurer of the Commonwealth of Virginia;
- f) Repurchase Agreements with Virginia banks acting as principal or agent, collateralized by U.S. Treasury/Agency securities. The collateral will at all times be no less than 100% of the value of the repurchase agreement.

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- g) Commercial paper of prime quality with a Standard and & Poor's Inc. rating not lower than A-1 or a Moody's Investors Service, Inc. rating not lower than P-1 for maturities of one year or less, and a rating of at least AA by Standard & Poor's and Aa by Moody's Investor Service, Inc. for maturities over one year and not exceeding five years.**
- h) Open-end investment funds (e.g., mutual funds), provided that the funds are registered under the Securities Act of the Commonwealth or the Federal Investment Co. Act of 1940, and that the investments by such funds are restricted to investments otherwise provided by law for political subdivisions.**

All investments will be in the name of the Town and will name the specific fund from which the instrument was purchased. Safekeeping account receipts will be held by the Finance Department or designated custodial agent.

BANKS AND DEALERS: SELECTION

Before accepting funds or engaging in investment transactions with the Town, the supervising officer at each depository and recognized securities broker/dealer shall submit a certification. The document will certify that the officer has reviewed the Town's investment policies and objectives and agrees to disclose potential conflicts or risks to public funds that might arise out of business transactions between the firm/depository and the Town.

Employees of any firm or financial institution offering securities or investments to the Town shall be trained in the precautions appropriate to public-sector investments and shall be required to familiarize themselves with the Town's investment objectives, policies and constraints.

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DIVERSIFICATION

The Town will diversify use of investment instruments to minimize risks due to a concentration in specific instruments, individual financial institutions, or maturities.

| <u>Diversification by Instrument:</u> | Maximum Percent Contained in Town's Investment Portfolio |
|---|---|
| U.S. Treasury Obligations (bills, notes and bonds) | 100% |
| U.S. Government Agency Securities and Instrumentalities of Government Sponsored Corporations | 100% |
| Open-end Investment Funds (mutual funds) | 100% |
| Banker's Acceptances (BAs) | 50% |
| Repurchase Agreements (Repos) | 25% |
| Certificates of Deposit (CDs) Virginia Qualified Commercial Banks/Savings and Loan Association | 75% |
| Local Government Investment Pool | 100% |
| Commercial Paper | 35% |

Diversification by Financial Institution:

| | |
|--|---|
| Banker's Acceptances (BAs) | Not more than 25% of the Town's total portfolio may be invested with any one institution |
| Repurchase Agreements (Repos) | Not more than 10 percent of the Town's total portfolio may be invested with any one institution |
| Certificates of Deposit (CDs) – Commercial Banks/Savings and Loan Associations | Not more than 33% of the Town's total portfolio may be invested with any one institution |
| Commercial Paper | Not more than 5% of the Town's total portfolio may be invested with any one issuer |
| Local Government Investment Pool | No restrictions |
| Open-end Investment Fund | No restrictions |

No other types of investments are permitted.

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| U.S. Treasury Obligations (bills, notes and bonds) | 100% |
| U.S. Government Agency Securities and Instrumentalities of Government Sponsored Corporations | 100% |
| Open-end Investment Funds (mutual funds) | 100% |
| Banker's Acceptances (BAs) | 50% |
| Repurchase Agreements (Repos) | 25% |
| Certificates of Deposit (CDs) Virginia Qualified Commercial Banks/Savings and Loan Association | 75% |
| Local Government Investment Pool | 100% |
| Commercial Paper | 35% |

Diversification by Financial Institution:

| | |
|---|---|
| Banker's Acceptances (BAs) | Not more than 25% of the Town's total portfolio may be invested with any one institution |
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| Certificates of Deposit (CDs) – Commercial Banks/Savings and Loan Associations | Not more than 33% of the Town's total portfolio may be invested with any one institution |
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MATURITIES AND VOLATILITY

Investments of the Town's operating funds will be limited to instruments maturing within three to five years at the time of purchase. Maturity scheduling will be timed according to anticipated need and will be scheduled to coincide with projected cash flow needs.

Investment of capital project, long-term reserve and other escrow funds will be timed to meet contractors' payments; debt service or other anticipated financial obligations. In such cases, the Town may invest reserve and escrow funds in securities maturing up to ten years from the date of purchase. The average weighted maturity of the total portfolio (which includes operating, capital project, long-term reserve and escrow funds) shall not exceed five years.

LIQUIDITY

A portion of the portfolio shall be invested in instruments that can be liquidated with one day's notice to meet the Town's operating needs.

RISKS

No individual investment shall be undertaken that jeopardizes the capital position of the portfolio. All investments shall either bear the full faith and credit of the United States government or be fully collateralized or insured, as defined by the Virginia Security for Public Deposits Act, Sec.2.2-4400 through 2.2-4411 of the Code of Virginia or otherwise comply with the standards as described in this policy and Sec. 2.2-4500 through 2.2-4517 of the Code of Virginia.

SAFEKEEPING AND CUSTODY

To protect against potential fraud and embezzlement, the assets of the Town shall be secured through third-party custody and safekeeping procedures. Bearer instruments shall be held only through third-party institutions. Investment officials shall be bonded to protect the public against possible embezzlement, malfeasance, nonfeasance, or negligence. Collateralized securities, such as repurchase agreements, shall be delivered to the Town or third party agent. Unless prevailing practices or economic circumstances dictate otherwise, ownership shall be protected through third-party custodial safekeeping.

Revision date: November 24, 2004

Attachment A - Investment of Public Funds - Section 2.2-4500 through 2.2-4517, Code of Virginia

Attachment B - Virginia Security for Public Deposits Act - Section 2.2-4400 through 2.2-4411, Code of Virginia