



# HUNTSVILLE UTILITIES POLICY

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**Policy #:** FM-04

**Policy:** Investments, Cash, & Banking Management

**Purpose:** To enhance the financial performance of Huntsville Utilities (HU) while protecting the principal of its investments. It is intended to maximize the efficiency of HU' cash management system, for prudently investing company funds and provide guidelines for suitable investments. HU' cash management system is designed to monitor and forecast expenditures and revenues accurately, thus enabling the Chief Financial Officer (CFO) to invest funds to the fullest extent possible. The CFO shall attempt to obtain the highest yield, if all investments meet the criteria established for safety and liquidity and comply with the applicable requirements of state law and federal tax regulations.

**Scope:** This investment policy applies to the investment of available assets of all HU, legal name "City of Huntsville, Alabama, a municipal corporation of the State of Alabama d/b/a Huntsville Utilities", IRS name for banking purposes "The City of Huntsville Utilities", funds under the direct management of the CFO.

Investments held in any fund or account of a trust indenture (an "Indenture") of HU pursuant to which revenues of the Electric System, Gas System or Water System are pledged to secure payment of warrants or other debt obligations shall be made in accordance with the terms of the applicable Indenture. If the terms of the applicable Indenture are unclear or do not direct how amounts in a particular fund or account are to be invested, then such amounts shall be invested in accordance with the requirements of this policy.

Funds set aside to defease debt in conjunction with an advance refunding, amounts on deposit in any fund or account of an Indenture, and amounts held outside an indenture that constitute reserve or "sinking funds" referable to tax-exempt debt obligations will be invested in accordance with the appropriate bond documents or tax compliance certificate or agreement and not necessarily pursuant to the terms of this policy.

All investments of HU must be made in compliance with federal and state laws and in accordance with applicable legal interpretations. Investment of any tax-exempt borrowing proceeds and/or of any debt service funds must comply with the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder by the U.S. Department of Treasury.

**General Objectives:**



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Funds of HU will be invested in accordance with Ala. Code §11-81-19—11-81-21 (1975), and in accordance with the following objectives in order of priority:

1. **Safety of Capital:** Safety of principal is the foremost objective of the investment program. Investments of HU shall be undertaken to ensure preservation of capital in the overall portfolio.
  - A. **Credit Risk**-HU will minimize credit risk, the risk of loss due to the failure of the security issuer or guarantor, by:
    - Limiting investments to the t types of securities defined in this document.
    - Pre-qualifying the financial institutions, brokers/dealers, intermediaries, and advisers with which the utility will do business.
    - Diversifying the investment portfolio so that potential losses on individual securities will be minimized.
  - B. **Interest Rate Risk**-HU will minimize the risk that the market value of securities in the portfolio will fall due to changes in general interest rates, by:
    - Structuring the investment portfolio so that securities mature to meet 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, money market funds, certificates of deposit, or similar investment pools.
2. **Liquidity:** The investment portfolio will remain liquid to meet all reasonably anticipated operating requirements. This is accomplished by structuring the portfolio to ensure securities mature concurrent with cash needs to meet anticipated demands. Furthermore, since not all possible cash demands can be anticipated, the portfolio should consist largely of securities with active secondary or resale markets. A portion of the portfolio also may be placed in money market mutual funds that offer same-day liquidity for short-term funds.
3. **Return on Investment:** The investment portfolio shall be designed with the objective of attaining a market rate of return relative to the prevailing demand deposit rate 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 be generally held until maturity with the following exceptions:
  - a) An investment with declining credit may be sold early to minimize loss of principal.
  - b) An investment swap would improve the quality, yield, or target duration in the portfolio.
  - c) Liquidity needs of the portfolio require that the investment be sold.
4. **Maintain the Public Trust:** All participants in the investment process shall seek to act responsibly as custodians of the public trust. Investment officials shall recognize that the



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investment portfolio is subject to public review and evaluation. In addition, the overall investment program shall be designed and managed with a degree of professionalism worthy of the public trust. Investment officials shall avoid any transaction that might knowingly impair public confidence in HU.

### Standard of Care:

1. **Prudence:** The standard of prudence used by investment officials shall be the “prudent person” standard and shall be applied in the context of managing an overall portfolio. Investment officers acting in accordance with written 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.

Investments shall be made with judgment and care, under circumstances that are prevailing, which persons of prudence, discretion, and intelligence exercise in managing 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.

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. To avoid the appearance of potential conflict of interest or favoritism to a particular bank or broker, the CFO or any delegated employee who has investment responsibilities shall make full written disclosure of any relationship or dealings with any financial institution that has business dealings with HU. This written disclosure will be filed with the President and CEO. This disclosure need not include normal banking or brokerage relationships that are at normal market rates and conditions available to the public. Employees and investment officials 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.
3. **Delegation of Authority:** Responsibility for the operation of the investment program is hereby delegated to the CFO, who shall act in accordance with established written procedures and internal controls for the operation of the investment program consistent with this investment policy. The CFO shall be responsible for all transactions undertaken, including the opening and closing of bank and investment accounts, and transfers between such accounts to maintain appropriate balances for cash management and investing activities. The CFO shall establish a system of internal controls as documented in the HU Treasury narrative. HU will maintain at least two of the following employees as signers on accounts: the CFO, Controller and/or President & CEO.

### Safekeeping and Custody:



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1. **Authorized Financial Dealers and Institutions:** The CFO will maintain a list of financial institutions authorized to provide investment services. Authorized financial institutions include banks maintaining an office in the state of Alabama and securities brokers/dealers classified by the New York Federal Reserve as primary dealers. Institutions will be evaluated annually on credit worthiness and other criteria as determined by the Finance Director. A list of authorized institutions will be established and maintained.
2. **Internal Controls:** The CFO is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of HU are protected from loss, theft, or misuse. (See the HU Treasury Narrative for detailed internal control processes.) The internal control structure shall be designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that:
  - a) The cost of a control should not exceed the benefits likely to be derived and,
  - b) The valuation of costs and benefits requires estimates and judgments by management.
3. **Delivery versus Payment:** All trades, where applicable, will be executed by delivery verses payment (DVP) to ensure that securities are deposited in an eligible financial institution prior to releasing funds. Securities will be held by a third-party custodian as evidenced by safekeeping receipts.

### Suitable and Authorized Investment:

1. **Investment Types:** The CFO is authorized to only invest HU funds in investments currently authorized by Alabama state law. This policy may further restrict the type of investments allowed for HU, but it cannot allow any additional investment types other than those authorized by current Alabama state law. The current Ala. Code §11-81-19—11-81-21 (1975) authorizes the investment in the following types of securities:
  - a) Direct obligations, including obligations issued or held in book entry form on the books the Department of the Treasury of the United States of America.
  - b) Obligations of any of the following federal agencies, which obligations represent the full faith and credit of the United States of America, Farmers Home Administration, General Services Administration, U.S. Maritime Administration, Small Business Administration, Government National Mortgage Association (GNMA), U.S. Department of Housing and Urban Development (HUD) and Federal Housing Administration (FHA).
  - c) U. S. dollar-denominated deposit accounts and certificates of deposit with banks or savings associations, including IntraFi sweep accounts (formerly CDARS and ICS deposit products), which are qualified public depositories under Chapter 14A of Title 41 if over FDIC insured limits.
  - d) Pre-refunded public obligations, defined as follows:
    - i. Any bonds or other obligations of any state of the United States of America or of any agency, instrumentality or local governmental unit of any such state (i) which are not callable at the option of the obligor prior to maturity or as to which irrevocable notice has been given by the obligor to call on the date specified in the notice, and (ii) which are fully secured as to principal and interest and redemption premium, if any, by a fund consisting only of cash or obligations



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described in subdivision (1) above, which fund may be applied only to the payment of such principal of and interest and redemption premium, if any, on such bonds or other obligations on the maturity date or dates thereof or the specified redemption date or dates pursuant to such irrevocable instructions, as appropriate, and (iii) which fund is sufficient, as verified by an independent certified public accountant, to pay principal of and interest and redemption, if any, on the bonds or other obligations described in this paragraph on the maturity date or dates thereof or on the redemption date or dates specified in the irrevocable instructions referred to in sub clause (i) of this paragraph, as appropriate, and (iv) which are rated, based on the escrow, in the highest rating category of Standard & Poor's Corporation and Moody's Investors Service, Inc., or any successors thereto.

- e) Interests, however evidenced, in any common trust fund or other collective investment fund maintained by any national or state chartered bank, trust company or savings association having trust powers, or securities of or other interests in any open-end or closed-end management type investment company or investment trust registered under the Investment Company Act of 1940, as from time to time amended, so long as all of the following requirements are met at the time of purchase and during the term of investment: (i) At least 65% of the portfolio of such common trust fund, collective investment fund or investment company or investment trust must consist of investments authorized in subdivisions (A), (B), (C), or (D) above, and (ii) the remainder of the portfolio (if any, but not more than 35%) may consist only of the following investments: (x) obligations issued or guaranteed by the following agencies: Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), including FNMA, and FHLMC participation certificates, Federal Land Banks, Central Bank for Cooperatives, Federal Intermediate Credit Banks, Student Loan Marketing Association, and
- f) Federal Home Loan Banks, (y) mortgage related securities (as that term is defined in Section 3(a) (41) of the Securities Exchange Act of 1934 (15 U.S.C.78c(a) (41)), or (z) repurchase agreements fully collateralized by obligations, securities or investments otherwise authorized under subdivisions 5(i)-(ii), so long as the common trust fund, collective investment fund, investment company or investment trust takes possession and delivery of the collateral for any repurchase agreement either directly or through an authorized custodian. The fact that any financial institution making such investment on behalf of the municipality or county, or any affiliate of such financial institution, is providing services to the investment company or investment trust as an investment advisor, sponsor, distributor, custodian, transfer agent, registrar, or otherwise, and is receiving reasonable remuneration for such services, shall not preclude such institution from making the investment in the securities of such investment company or investment trust; provided, however, that with respect to any account for municipal funds or county funds to which fees are charged for such services, the said financial institution shall disclose (by prospectus, account statement or otherwise) to the beneficiary of such account or to any third party directing investments the basis (expressed as a percentage of asset value or otherwise) upon which the fee is calculated.



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- 2. Collateralization:** If over FDIC insured limits, it is HU policy that any bank or financial institution in the State of Alabama that invest utility funds shall be a Qualified Public Depository certified by the Alabama State Treasurer according to the Security for Alabama Funds Enhancement (SAFE) Act, Ala. Code §41-14A-1 et seq., (1975).

All deposits made and certificates of deposit (CDs) issued in excess of amounts insured by the FDIC and FSLIC shall be collateralized with securities of the United States government, federal agencies that represent the full faith and credit of the United States, or otherwise authorized by state law. The collateral for each deposit or certificate of deposit shall have a market value equal to at least 100 percent of the excess of amounts insured by the FDIC and FSLIC.

It is the policy of HU to require from each authorized financial institution holding utility funds a listing of securities pledged as collateral to protect utilities investment. This listing of collateral shall be provided to HU by each institution for deposits held on June 30 and December 31 of each year. All investment securities purchased by HU and all collateral on deposits of the utility shall be held in a custodian account maintained by a trust department of a bank insured by the FDIC, in the Federal Reserve Bank or by HU. The trust department shall issue a safekeeping receipt to the utility listing the specific instrument, rate of return, maturity date and other pertinent information.

### Investment Parameters:

- 1. Diversification:** HU will diversify its investments by security type and institution. With the exception of U.S. Treasury securities, no more than 50% of the utilities total investment portfolio will be invested in a single security type, and no more than 50% with a single financial institution.
- 2. Mutual Funds:** HU will only make direct investments in obligations, bonds, notes, debentures or other evidence of indebtedness issued and guaranteed by the following agencies Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), including FNMA, and FHLMC participation certificates, Federal Land Banks, Central Bank for Cooperatives, Federal Intermediate Credit Banks, Student Loan Marketing Association, and Federal Home Loan Banks. Investments such as mutual funds, common trust funds or other collective investment funds are not allowed by this policy, unless as identified in section 1(e) maintained by any national or state chartered bank, trust company or savings association having trust powers.
- 3. Bauer Financial Star Rating:** HU will only make investments and deposits over the FDIC insured limits in financial institutions that meet all other requirements of this policy and have a Bauer Financial Star Rating of no less than three stars.
- 4. Maximum Maturities:** To the extent possible, HU shall attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the utility will not directly invest in securities maturing more than five (5) years from the date of purchase.

Because of inherent difficulties in accurately forecasting cash flow requirements, a portion of the portfolio should be continuously invested in readily available funds such as local



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government investment pools, money market funds, or overnight repurchase agreements to ensure that appropriate liquidity is maintained to meet ongoing obligations.

### Reporting:

- 1. Methods:** The CFO shall submit a monthly investment report to the President and CEO and quarterly reports to the Electric, Gas, and Waterworks Boards. The report shall include a general description of the portfolio in terms of investment securities, maturities, yields and other features. The report will show investment earnings for the month and fiscal year-to-date, including the annualized earned yield percentage for the portfolio. The report will compare actual investment earnings with budgeted earnings.

### 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. Given the passive type of investment strategy the utility uses, the basis used to determine whether market yields are being achieved shall be the one-year Constant Maturity Treasury Rate.

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