

Construction and Use of Common Fiscal Policies



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The webinar will begin at 10:00 a.m. CST



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About the Speaker



Benjamin Hart

- Provides dual insights of a governmental CFO along with experience of governmental auditing for a public accounting firm
- Brings extensive expertise in governmental budgeting, financial and internal controls, public sector leadership and more
- Consistently earned the GFOA certificate for Excellence in Financial Reporting with his CAFRs

Agenda

- The basics of policy
 - What they are and aren't
 - Why they are important
 - Who the stakeholders in the policy might be
 - What makes it strategic
- Cash management & investment
 - Policy impact on use of resources
- Debt management and reserves

Polling Question #1

Case 1 – The Problem



Case 1 – The Problem

- City of 150,000 – “hyper-growth”
- 64 square miles
- Sales tax ½ budget resource
 - New retail
 - New residential growth
- Collections outpace expenses
- Use of debt – proceeds deposited

Case 1 – The Solution

- Committee/task force of EO and staff
- Cash management & investment policy
- Maximize return on funds
- Provide for safety of principal
- Invest in the local financial institutions

What Policies Aren't

- A set-it-and-forget-it tool
- A summation of regulations governing specific decisions
- A document drafted, discussed, and implemented by a party of one!
- A “quick fiscal fix”
- Just more **red tape**

What They Are

- Written, written, written
- In plain language
- Transparent and accessible
- A complement to strategic plans
- Definition of specific elements
- A complement to procedures
- Created with a built-in expiration

“It’s not that you have to know every single debit and credit, but you have to have an understanding of when something just doesn’t sound right.”

*--Kinney Poynter, Executive Director,
National Association of State Auditors,
Comptrollers and Treasurers*



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Definitions

- a) A definite course or method of action selected from among alternatives and in light of given conditions to guide and determine present and future decisions...*
- b) A high-level overall plan embracing the general goals and acceptable procedures especially of a governing body.*

-- Merriam-Webster

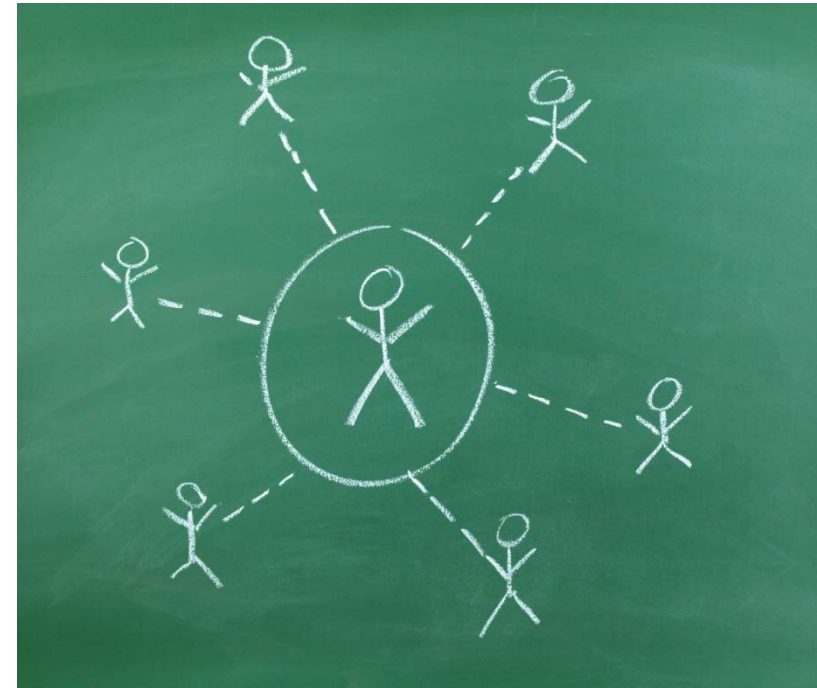
Why They Are Important

- Institutionalize
- Clarify and “crystallize”
- Boundaries
- Bond ratings
- Long-term thinking
- Risk to financial condition
- Best practices



The Stakeholders

- Bond investors
 - Bond-rating agencies
- Commercial taxpayers
- Residents
- Governing body
- Departmental staff



Polling Question #2

How are “Policies” Strategic?

- Be “entity-relevant”
- Long-term outlook on current issues
- Provide guidance on aligning strategic resources with priorities
- Include benchmarks or measures, good and bad
- Enable improvement (is bond rating the only one?)

Essential Vs. Highly Advisable

Essential Policies

- Fund balance and reserves
- Operating budget
- Capital budgeting and planning
- Debt management
- Long-range financial planning
- Investment

Highly Advisable Policies

- Accounting & financial reporting
- Revenues
- Internal controls
- Expenditures
- Purchasing
- Risk management
- Economic development

Cash Management and Investments

“An investment policy should describe the most prudent primary objectives for sound policy; safety, liquidity, and yield.”

**--GFOA Best Practice,
Oct. 2010**



Case 2 – The Problem



Case 2 – The Problem

1. Finance director employed for 15 years
2. Interest income sporadic/principal stable
3. No, if any reporting
4. Investments found to be purchased from bank of India, bank of Dubai, bank of China
5. Collateralization requested by auditors, not something that was monitored.

Case 2 – The Solution

- Audit of the former investment policy
- Review against state-permissible investments
- Policy renewal debate with governing body – included controls and reporting

What's the Point? Making the Case

- Common definitions
 - Types of Investments (permitted and prohibited)
 - Risks
- Who does what?
- Concrete guidelines
- Balancing liquidity with potential earnings
- Diversification (market and rate risk)

Polling Question #3

Major Components

- Scope –
 - *Not held with fiscal agents or trustees*
 - *Debt service fund trust accounts*
 - *Reserve funds*



Major Components

- Authority
 - Mgmt. responsibility for investments delegated to Director of Resource Mgmt. (Investment Officer/IO)
 - IO to establish/maintain written procedures for cash and investment program
 - Explicit delegation of authority to persons responsible for investment transactions
 - No investment transactions except as per this policy and procedures set by IO

Major Components

- Authority – continued
 - Investment advisor: City may engage external advisors to help management portfolio consistent with City objectives
 - Advisors may be granted discretion to buy or sell securities consistent with investment policy for up to 50% of City portfolio.
 - Requirements and criteria for investment advisors

Major Components

- Objectives
 - Safety is the foremost objective
 - Invest to protect principal and interest and avoid capital losses
 - Mitigate credit and interest rate risk
 - Liquidity to meet all operating requirements
 - Portfolio structured to match securities maturity with cash flow and cash flow fluctuations
 - Liquidity is a priority, while recognizing the need to maximize yield.

Major Components

- Standards of care
 - “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”*

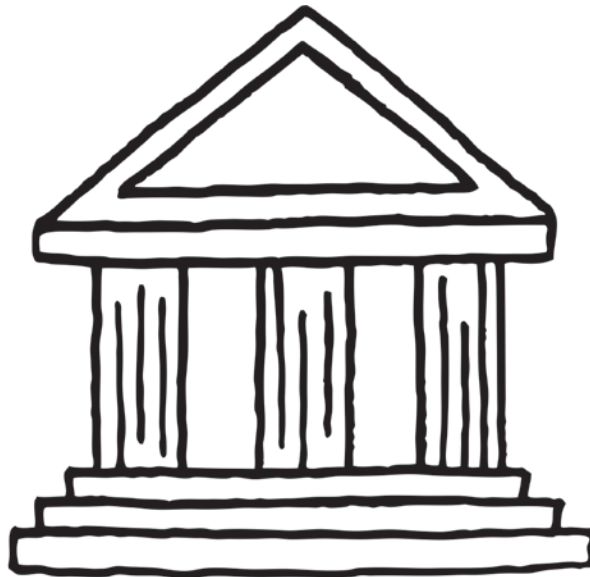
Major Components

- Standards of care
 - Prudent investor rule
 - Ethics and conflict of interest
 - Public trust statement
 - Term – (maximum)
 - Cash flow
 - Segregation of duties
 - Liability



Major Components (cont'd)

- Authorization of Institutions
 - Institutions authorized to provide investment services and approved security broker/dealers
 - Selected by creditworthiness and additional criteria



Major Components (cont'd)

- Authorization of Institutions
 - Financial institutions seeking qualification for investment transactions must provide:
 - Audited financial statements;
 - For Broker/Dealers – FINRA certification, state registration w/ state Securities Commission, registration w/ bank regulatory organization
 - Qualifications of individuals providing services
 - Certification that the financial institution and/or broker/dealer will comply with investment policy

Major Components (cont'd)

- Permitted vs prohibited investments
 - *Prohibited: inverse floaters, range notes, interest-only strips derived from a pool of mortgages (collateralized mortgage obligations), and any security that could result in zero interest accrual if held to maturity*



Major Components (cont'd)

- Investment parameters
- Safekeeping and custody
- Reporting and review
- Expiration of policy



Making It Strategic

- Investment maturity -
 - Adherence to local law (investment authority beyond the law)
- Maximize returns & provide liquidity
- Supporting local economy
 - CRA involvement
- National rankings of the institution
 - Annual review

Polling Question #4

Authoritative Resources

- Government Finance Officers Association
- Association of Public Treasurers of the US & Canada

Thank You!

Ben Hart



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