



## TEXAS WATER TRADE INVESTMENT POLICY

### I. PURPOSE AND SCOPE

This investment policy applies to the investment activities of Texas Water Trade (“TWT”). The purpose of this investment policy is to provide guidance to the Board of Directors of TWT, staff, and investment manager(s) regarding the investment of TWT funds and the use of investment income. A Finance and Investment Committee shall be established and be charged with the responsibility of implementing the Board-approved investment policies and overseeing their implementation. Any amendments to this investment policy will require approval of the Board of Directors.

### II. OBJECTIVES

This investment policy is designed to address the following: (A) state in a written document the investment objectives and management guidelines for the appointed Finance and Investment Committee to implement and monitor; (B) establish an investment framework for the management of TWT’s various investment accounts, with the framework to include guidelines as to asset class, investment styles and strategies, and asset allocation ranges which are expected to produce a sufficient level of diversifications and investment return over the long-term; and (C) establish criteria to monitor, evaluate, and compare performance results on a regular basis.

All participants in the investment process shall seek to act responsibly as fiduciaries of the assets of TWT. Investment officials shall avoid any transactions that might impair public confidence in TWT’s ability to manage its funds effectively. The Board of Directors recognizes that in a diversified portfolio, occasional measured losses due to market volatility are inevitable and must be considered within the context of the overall portfolio’s investment return, provided that adequate diversification has been implemented.

TWT’s investment objectives have been established in conjunction with a comprehensive review of the current and projected financial requirements of TWT. TWT may manage multiple different investment accounts, each with its own funding needs, investment requirements, and investment strategy. Funds received for these separate uses may have different investment requirements due to the liquidity needs of TWT, expected terms of their investment, and the acceptable risk and volatility during their term. Moreover, individual donor specifications or restrictions may create additional investment requirements or restrictions. TWT currently receives or may receive contributions for the Operating, Capital, and Reserve Accounts described below. The guiding principles of this investment policy and its implementation for funds held in the Operating, Capital, and Reserve Accounts are, in order of priority, safety of principal, liquidity, diversification, and yield. In addition, in anticipation of potential future endowment opportunities, the TWT Board of Directors has also developed objectives for an Endowment Account.

### III. FUNDS AND ACCOUNTS

#### *Operating Account*

The purpose of the Operating Account is to fund TWT programs and provide unrestricted income for support services. The investment strategy is to invest funds in short-term investments, with cash required immediately to within twelve months. Risk of the investments shall be low to protect the value of principal as a priority while earning a modest rate of return. The investments shall be short-term to medium-term, liquid investments that maximize safety while providing a modest investment return. Investment grade securities are required to be eligible for investment funds in the Operating Account. Investment income shall be used for unrestricted support services and may be distributed 100% annually, unless otherwise restricted by donors.

#### *Capital Account*

The purpose of the Capital Account is to provide funds for the Texas Flows Fund, a TWT administered capital program. The investment strategy is to invest funds in medium-term investments, with funds expected to be expended within one to four years. Risk of the investments shall be low to protect the value of principal as a priority while earning a modest rate of return. The investments shall be short- to medium-term, liquid investments that maximize investment earnings while protecting principal. Investment grade securities are required to be eligible for investment funds in the Capital Account. Investment income shall be reinvested until required for funding the cost of capital projects.

#### *Reserve Account*

The purpose of the Reserve Account is to provide funds for such needs as addressing an annual funding shortfall, a strategic financial need, and/or providing needed additional security for soliciting future contributions. The investment strategy is to invest funds in medium-term investments, but shall remain available for TWT financing needs, with a term of three years or less. The investments shall be in short- to medium-term, liquid investments that maximize investment earnings while protecting principal. Investment grade securities are required to be eligible for investment funds in the Reserve Account. Investment income may be distributed 100% annually to fund operations.

#### *Endowment Account*

The purpose of the Endowment Account is to manage funds in support of the long-term operations and programs of TWT. The investment strategy is to invest funds in long-term investments, of a duration of no more than ten years, unless otherwise a longer term is approved by the Board of Directors. The investments shall seek growth of the real (inflation-adjusted) market value of endowment assets in order to meet the policy objectives described below. In addition, volatility in endowment asset value shall be

managed through an investment portfolio, whose diversity shall be addressed through market geography, investment style and strategy, and asset class.

The Board of Directors may consider the distribution of not more than 4% of the trailing 12-quarter average value of the Endowment Account to support current operations. During endowment-building campaigns, however, distributions may be calculated on the fiscal year ending balance of the endowments, in lieu of the average value over the trailing 12 quarters, in order to maximize immediate program impact. Other amounts may be distributed, but not before advance approval by the Board of Directors, and not before the long-term effects of such additional distributions have been carefully considered and vetted.

The asset allocations of funds in the Endowment Account are:

	<u>Allowable Range</u>	<u>Strategic Target</u>
Cash & Cash Equivalents	0% to 10%	0%
Debt Securities	20% to 50%	30%
Equity Securities	40% to 80%	70%

Note: all allocations are expressed as percentages of total portfolio

Equity and equity-like securities may include large and small cap stocks listed on domestic U.S. markets. TWT may fulfill investment requirements through a combination of individual equities, mutual funds, exchange traded funds, or market index funds. Debt instruments purchased as individual securities (with the exception of mutual funds and exchange traded funds) shall be investment grade with securities downgraded by one full rating level (e.g., AA to A) to be sold as soon as practical.

The performance of the overall endowment portfolio will be measured against a benchmark of 70% of the S&P 500 Index and 30% of the *Merrill Lynch Three to Five Year Treasury Index*. Individual managers shall be measured against the appropriate benchmark specific to the manager's stated approach. The performance evaluation of the managers shall be considered over a period of three years.

#### IV. INVESTMENT MANAGERS

The Board may contract with an investment management firm to provide for the investment and management of funds under its control. The investment management firm must be registered either under the Investment Advisers Act of 1940 or with the Texas State Securities Board. The contract with the investment management firm shall be limited to a maximum term approved by the Board of Directors. The Board may designate an employee of its contracted investment management firm as Investment Officer in addition to any member or members of the Board.

The Board's approved investment policy shall govern the management of its funds. No persons may engage in an investment transaction except as provided under the terms of this policy and any written procedures established by the Board. An annual compliance

audit of management controls on investments and adherence TWT's established investment policies will be undertaken in conjunction with the annual financial audit.

TWT shall require and provide investment training for Investment Officers designated by the Board in order to ensure the quality and capability of investment management. Training will be provided through courses and seminars offered by independent sources approved by the Board. Investment Officers shall receive a minimum amount of investment training as determined by the Board from an approved source within 12 months of appointment or assumption of duties. Investment officers shall receive continuing investment training as determined by the Board from an approved source no less often than every two years after receiving initial training.

The Board of Directors shall receive an investment report containing all information related to investment activity no less often than twice a fiscal year. As part of the report, all Board-designated Investment Officers shall sign a statement of compliance of the investment portfolio with the investment strategies stated in this investment policy.

Investments shall be made with judgment and care, under prevailing circumstances, that a person of prudence, discretion and intelligence would exercise in the management of the person's own affairs, not for speculation, but for investment, considering the probable safety of capital and the probable income to be derived.

An Investment Officer who has a personal business relationship with a business organization offering to engage in an investment transaction with TWT or a business organization offering to contract with TWT for investment management services shall file a statement disclosing that personal business relationship. An Investment Officer who is related within the second degree by affinity or consanguinity, as determined under Chapter 573, Texas Government Code, either to an individual seeking to sell an investment to TWT or to an individual representing an investment management firm offering to contract with TWT for investment management services, shall file a statement disclosing that relationship. The required disclosure statements shall be filed with the Board.

#### V. AUTHORIZED AND SUITABLE INVESTMENTS

Funds held in the Operating Account, the Capital Account and the Reserve Account may be invested in the instruments described in Appendix A. Funds in the Endowment Account may be invested as described in this investment policy. Investments not otherwise authorized by this investment policy are prohibited.

#### APPROVALS BY THE BOARD OF DIRECTORS

The above policy and Exhibit A were accepted and approved by vote of the Texas Water Trade Board of Directors on May 14, 2020.

## EXHIBIT A

(1) Federal Securities, consisting of direct, noncallable obligations of the United States of America, including obligations that are unconditionally guaranteed by the United States of America;

(2) Investment Agreements, consisting of: (a) any investment agreement with financial institutions whose long-term obligations are rated within the top two rating categories (without regard to gradations within the rating category) of any nationally recognized rating service or whose short-term obligations are rated within the top rating category of any nationally recognized rating service; (b) any investment agreement rated within the top two rating categories of any nationally recognized rating service; and (c) any investment agreement fully secured by Federal Securities;

(3) Demand deposits, including interest bearing money market accounts, time deposits, trust funds, trust accounts, overnight bank deposits, interest-bearing deposits, other deposit products, certificates of deposit, including those placed by a third party, or bankers acceptances of depository institutions;

(4) The following bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following federal agencies and provided such obligations are backed by the full faith and credit of the United States of America (stripped securities being permitted only if they have been stripped by the agency itself): (i) direct obligations or fully guaranteed certificates of beneficial ownership of the United States Export-Import Bank, (ii) participation certificates and guaranteed pool certificates of the Small Business Administration; (iii) debentures of the Federal Housing Administration; (iv) guaranteed mortgage-back bonds and guaranteed pass-through obligations of the Government National Mortgage Association; and (v) project notes, local authority bonds, guaranteed debentures and guaranteed public housing notes and bonds of the United States Department of Housing and Urban Development;

(5) The following bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following non-full faith and credit United States government agencies (stripped securities being permitted only if they have been stripped by the agency itself): (i) senior debt obligations of the Federal Home Loan Bank System; (ii) participation certificates and senior debt obligations of the Federal Home Loan Mortgage Corporation; (iii) mortgage-backed securities and senior debt obligations of the Federal National Mortgage Association; (iv) obligations of the Resolution Funding Corporation; and (v) obligations of the Federal Farm Credit Banks Funding Corporation;

(6) Money market funds registered under the Investment Company Act of 1940, the shares of which are registered under the Securities Act of 1933, and having a rating of no less than "AA" or its equivalent from a nationally recognized rating agency;

(7) Commercial paper, with a maturity not greater than 270 days, and rated, at the time of purchase, "Prime-1" by Moody's, "F1" or better by Fitch or "A-1" or better by S&P;

(8) General obligation bonds, notes or other obligations of states that are rated within the top two rating categories (without regard to gradations within the rating category) from a nationally recognized rating agency; and

(9) Federal funds or bankers' acceptances with a maximum term of one year of any bank which has an unsecured, uninsured and unguaranteed obligation rating of "A-1/Prime-1" or "Aa3" or better by Moody's and "F1" or "A" or better by Fitch and "A-1" or "A" or better by S&P at the time of the investment.

Ratings shall be determined at the time of purchase, and without regard to rating subcategories.