

# EXHIBIT A



## CITY OF POMONA FISCAL YEAR 2018-2019 STATEMENT OF INVESTMENT POLICY

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ADOPTED BY CITY COUNCIL  
RESOLUTION NO. 2018-XX  
JULY 16, 2018

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## **I. MISSION STATEMENT**

It is the policy of the City of Pomona ("City") to invest public funds in a manner that will provide maximum security, adequate liquidity and sufficient yield, while meeting the daily cash flow demands of the City and conforming to all statutes and regulations governing the investment of public funds.

## **II. INTRODUCTION**

The City of Pomona investment program will conform to federal, state, and other legal requirements, including California Government Code Sections 16429.1-16429.4, 53600-53609 and 53630-53686. The following investment policy addresses the methods, procedures and practices which must be exercised to ensure effective and judicious fiscal and investment management of the City's funds.

This investment policy was endorsed and adopted by the City's governing body and is effective as of the 16<sup>th</sup> day of July, 2018. This Investment Policy replaces any previous Investment Policy or Investment Procedures of the City.

## **III. SCOPE**

This investment policy applies to all the cash assets of City of Pomona, the Pomona Housing Authority, the Pomona Public Financing Authority, and the Successor Agency of the City of Pomona. These funds are accounted for in the City's audited Annual Financial Report. If the City invests funds on behalf of another agency and, if that agency does not have its own policy, the City's investment policy shall govern the agency's investments.

### **A. Pooling of Funds**

Except for cash in certain restricted and special funds, the City shall consolidate cash balances from all funds to maximize investment earnings and to increase efficiencies with regard to investment pricing, safekeeping and administration. Investment income shall be allocated to various funds in accordance with generally accepted accounting principles.

### **B. Funds Included in this Policy**

The funds subject to this policy are: General Fund; Special Revenue Funds; Capital Project Funds; Enterprise Funds; Internal Service Funds; Trust and Agency Funds; and any new fund that may be created unless specifically exempted.

### **C. Funds Excluded from this Policy**

1. City's Service Retirement System Fund. This fund is managed by the California Public Employee's Retirement System (CalPERS).
2. Deferred Compensation Funds. Both the regular deferred compensation plan and the City's Hourly/Part-time Employee Retirement Plan are invested in accordance with its trust fund agreement.
3. City's Postemployment Benefits Plan. These funds are managed by PARS and are related to the collateral benefit program provided through employee MOUs.
3. Bond Proceeds. Investment of bond proceeds shall be subject to the conditions and restrictions of bond documents and are not governed by this policy.

#### **IV. GENERAL OBJECTIVES**

The overriding objectives of the investment program are to preserve principal, provide sufficient liquidity, provide sufficient investment yield, and manage investment risks.

##### **A. Safety**

Preservation of principal is the foremost objective of the investment program. Investments of the City shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective shall be to mitigate credit risk and interest rate risk. To attain this objective, the City shall seek to diversify its investments by investing funds among several financial institutions and a variety of securities offering independent returns.

###### **1. Credit Risk**

The City shall minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

- Limiting investments to the most creditworthy types of securities
- Pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisers with which the City will do business
- By diversifying the investment portfolio so that the potential failure of any one issue or issuer will not place an undue financial burden on the City

###### **2. Interest Rate Risk**

To minimize the negative impact of material changes in the market value of securities in the portfolio, the City shall:

- Structure the investment portfolio so that securities mature concurrent with cash needs to meet anticipated demands, thereby avoiding the need to sell securities on the open market prior to maturity
- Invest operating funds primarily in shorter-term securities, money market mutual funds, and the State of California's Local Agency Investment Fund ("LAIF")

##### **B. Liquidity**

The City's investment portfolio shall remain sufficiently liquid to enable the City to meet all operating requirements that might be reasonably anticipated without requiring a sale of securities.

##### **C. Yield (Return on Investment)**

The City's investment portfolio shall be designed with the objective of attaining a benchmark rate of return throughout budgetary and economic cycles, commensurate with the City's investment risk constraints and the liquidity characteristics of the portfolio. 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.

#### **V. STANDARDS OF CARE**

##### **A. Prudence**

The standard of prudence to be used by City investment officials shall be the "prudent investor standard" (California Government Code Section 53600.3) in that a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including,

but not limited to, the general economic conditions and the anticipated needs of the City, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of an enterprise of a like character and with like aims. This standard shall be applied in the context of managing the overall portfolio. City investment officers acting in accordance with written procedures and the 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 appropriate action is taken to control adverse developments.

**B. Indemnification**

The City Treasurer and other authorized persons responsible for managing City funds, acting in accordance with written procedures and the Investment Policy and exercising due diligence, will be relieved of personal responsibility for an individual security's risk or market price changes, provided deviations from expectations are reported within 30 days and appropriate action is taken to control adverse developments.

**C. Ethics and Conflicts of Interest**

Officers and employees involved in the City investment process shall refrain from personal business activity that could conflict with proper execution of the investment program, or that could impair their ability to make impartial investment decisions. City employees and investment officials shall disclose any material financial interests in financial institutions that conduct business within their jurisdiction, and they shall further disclose any personal financial/investment positions that could be related to the performance of the City immediately to the Pomona City Treasurer and annually to the Fair Political Practices Commission. City employees and officers shall refrain from undertaking personal investment transactions with the same individual with whom business is conducted on behalf of the City.

**D. Delegation of Authority**

Authority to manage the City's investment program is derived from Sections 704 and 705 of the Charter of the City of Pomona. In accordance with Section 704 (City Treasurer) the City Council shall appoint the City Treasurer who has the authority to invest or to reinvest funds, or to sell or exchange securities. Upon appointment, the City Treasurer shall thereafter assume full responsibility for those transactions until the delegation of authority is revoked or expires. By Charter (Sec 705), the Finance Director also has authority to receive and invest City funds.

The City may engage the services of one or more external investment managers to assist in the management of the City's investment portfolio in a manner consistent with the City's objectives. Such external managers may be granted discretion to purchase and sell investment securities in accordance with this Investment Policy. Such managers must be registered under the Investment Advisers Act of 1940.

**E. Procedures and Internal Controls**

Management responsibility for the investment program is delegated to the City Treasurer who shall establish a separate written investment procedures manual to assist investment staff with day-to-day operations of the investment program consistent with this policy. The procedures should include reference to: authorized personnel, safekeeping, master repurchase agreements, wire transfer agreements, banking service contracts, collateral/depository agreements, and cash flow forecasting. Such procedures shall include explicit delegation of authority to persons responsible for investment transactions. No person may engage in an investment transaction except as provided under the terms of this

policy and the procedures established by the City Treasurer. The operation of the investment program shall be consistent with this policy and the investment procedures manual.

The City Treasurer is responsible for establishing and maintaining a system of written internal controls. These controls shall be reviewed annually with an independent external auditor who will notify the City Council if there is a material non-compliance with its policies and procedures. The internal controls shall be designed to prevent losses of public funds arising from fraud, employee error, and misrepresentation by third parties, unanticipated changes in financial markets, or imprudent action by City employees and officers. The internal structure shall be designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived, and (2) the valuation of costs and benefits requires estimates and judgments by management.

#### **F. Review of Investment Portfolio**

The securities held by the City must be in compliance with Section VII Suitable and Authorized Investments at the time of purchase and at least quarterly. The City Treasurer shall establish procedures to report to the City Council, major and critical incidences of noncompliance identified through the review of the portfolio.

### **VI. AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS**

The Treasurer shall transact business only with Registered Investment Advisors, national or state-chartered banks, savings and loans, and broker dealers. The dealers should be primary dealers regularly reporting to the New York Federal Reserve Bank, or approved regional or secondary market dealers that qualify under the Securities and Exchange Commission Rule 15C3-1 (uniform net capital rule). The Treasurer shall formally authorize investment broker-dealers to provide investment services to the City and shall maintain a list of financial institutions so authorized to provide investment services. Audited financials, proof of Financial Industry Regulatory Authority (FINRA) certification, State of California registration, and certification of having read and understanding the City's Policy is required from approved advisors.

If a third party investment advisor is authorized to conduct investment transactions on the City's behalf, the investment advisor may use its own list of broker/dealers and financial institutions. The investment advisor's list must be available to the City upon request.

Public deposits will be made only in qualified public depositories as established by State law. Deposits will be insured by the Federal Deposit Insurance Corporation, or, to the extent the amount exceeds the insured maximum, will be collateralized in accordance with State law.

### **VII. SAFEKEEPING AND CUSTODY**

All security transactions, including collateral for repurchase agreements, entered into by the City shall be conducted on a delivery-versus-payment (DVP) basis which will ensure that securities are deposited in an eligible financial institution prior to the release of funds. Securities shall be held by a third-party custodian or broker/dealer designated by the City Treasurer. The only exception to the foregoing shall be depository accounts and securities purchases made with: LAIF, time certificates of deposit and money market mutual funds, since the purchased securities are not deliverable. City Treasurer shall be bonded to protect the public against possible embezzlement and malfeasance.

## VIII. SUITABLE AND AUTHORIZED INVESTMENTS

The City is governed by the California Government Code, Sections 53600 et seq. If the Code is amended to allow additional investments or is changed regarding the limits on certain categories of investments, the City is authorized to conform to the changes in the revised Code, provided that the changes are not specifically prohibited by the City's policy. The City shall be required to present those changes in the annual review of the policy and to incorporate the new legislation within the policy. Surplus funds are defined as funds not required for the immediate necessities of the City and include investments in individually managed portfolio(s), money market fund(s) and/or State LAIF, and all portfolio limitations and restrictions shall apply to this aggregate amount. For purposes of compliance with the California Government Code and the City's Investment Policy, the credit rating requirement for medium-term notes, deposit notes, bank notes and commercial paper shall be based on the quality ratings at the time of purchase. If the quality rating of the issuer is downgraded, subsequent to purchase, by any of the Nationally Recognized Statistical-Rating Organizations below "A", or its equivalent, it shall be reported to the City Council with a recommendation, and ongoing information shall be provided if the bond is not sold. Percentage limitations of surplus funds invested are noted for the various investment instruments. Where there is a specified percentage limitation for a particular category of investments, that percentage is applicable only at the date of purchase. A later increase or decrease in a percentage resulting from a change in values or assets shall not constitute a violation of that restriction.

The City is empowered by statute to invest in the following types of securities:

### A. Authorized Investment Summary Matrix

	<b>Investment Type</b>	<b>Maximum Maturity</b>	<b>Maximum Specified % of Portfolio</b>
1	City of Pomona Bonds	5 Years	No limit
2	U.S. Treasury Obligations	5 years	No limit
3	U.S. Agency Obligations	5 years	No limit
4	CA and Local Agency Obligations	5 years	No limit
5	Other State and Local Agency Obligations	5 Years	15%
6	Medium-Term Notes	5 Years	30%
7	Bankers' Acceptances	180 days	40%
8	Commercial Paper	270 days	25%
9	Negotiable Certificates of Deposit	5 years	15%
10	Time Deposits	5 years	10%
11	Savings Accounts	5 years	10%
12	Money Market Mutual Funds	n/a	15%
13	Repurchase Agreements	92 days	20%
14	Local Agency Investment Fund (LAIF)	n/a	No limit
15	Supranational	5 Years	30%



## Investment Types

1. Bonds issued by the City, including bonds payable solely out of the revenues from a revenue producing property owned, controlled, or operated by the City or by a department, board, agency, or authority of the local agency.
2. United States Treasury notes, bonds, bills, or certificates of indebtedness, or those for which the full faith and credit of the United States are pledged for the payment of principal and interest.
3. Federal Agency or United States government-sponsored enterprise obligations (GSE), participations, or other instruments.
4. State of California and Local Agency Obligations. Registered state warrants or treasury notes or bonds of this state, including bonds payable solely out of the revenues from revenue-producing property owned, controlled, or operated by the state or by a department, board, agency, or authority of the state; and bonds, notes, warrants, or other evidence of indebtedness of any local agency within this state including bonds payable solely out of the revenues from revenue-producing property owned, controlled, or operated by the local agency, or by a department, board, agency, or authority of the local agency. Notes eligible for investment shall be rated in a category of "A" or its equivalent or better by two Nationally Recognized Statistical-Rating Organizations.
5. Out-of-State and Local Agency Obligations. Registered treasury notes or bonds of any of the other 49 states in addition to California, including bonds payable solely out of the revenues from revenue-producing property owned, controlled, or operated by the state or by a department, board, agency, or authority of the other 49 states in addition to California; and bonds, notes, warrants, or other evidence of indebtedness of any local agency within this state including bonds payable solely out of the revenues from revenue-producing property owned, controlled, or operated by the local agency, or by a department, board, agency, or authority of the local agency. Notes eligible for investment shall be rated in a category of "A" or its equivalent or better by two Nationally Recognized Statistical-Rating Organizations.
6. Medium-Term Notes, defined as all corporate and depository institution debt securities with a maximum remaining maturity of five (5) years or less, issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States. Purchases of medium-term notes may not exceed 30% of the City's surplus funds. Investments in medium-term notes for any one non-government issuer shall be limited to no more than of surplus funds. Notes eligible for investment shall be rated in a category of "A" or its equivalent or better by two Nationally Recognized Statistical-Rating Organizations.
7. Bankers Acceptances otherwise known as bills of exchange or time drafts, drawn on and accepted by a commercial bank, which are eligible for purchase by the Federal Reserve System. Purchased bankers acceptances may not exceed one hundred and eighty (180) days maturity or 40% of the City's surplus funds, and no more than 5% of the City's surplus funds may be invested in the banker's acceptances of any one commercial bank.
  - a. They are issued by institutions with short term debt obligations rates "A1" or higher, or equivalent, by at least two nationally recognized statistical-rating organization ("NRSRO"); and have long-term debt obligations which are rated "A" or higher by at least two NRSRO.
8. Commercial Paper of "prime" quality of the highest ranking or the highest letter and number rating as provided for by a Nationally Recognized Statistical-Rating Organization.

The entity that issues the commercial paper shall meet all of the following conditions in either paragraph (a) or paragraph (b):

- a. The entity is organized and operating in the United States as a general corporation and has total assets in excess of five hundred million dollars (\$500,000,000). In addition, its debt other than commercial paper, if any, must be rated "A" or higher by a Nationally Recognized Statistical-Rating Organization.
- b. The entity is organized within the United States as a special purpose corporation, trust, or limited liability company and has a program-wide credit enhancement including, but not limited to, over-collateralization, letters of credit, or a surety bond. In addition, the entity has commercial paper that is rated "A-1" or higher, or the equivalent, by a Nationally Recognized Statistical-Rating Organization.

Eligible commercial paper shall have a maximum maturity of two hundred and seventy (270) days or less. The City may not invest more than 25% of its surplus funds in no more than 10% of the outstanding eligible commercial paper of any single issuer.

9. Negotiable Certificates of Deposit issued by a nationally or state-chartered bank or savings association or federal association or a state or federal credit union or by a state-licensed branch of a foreign bank. Purchases of negotiable certificates of deposit shall not exceed 15% of the City's surplus money invested and shall be limited to no more than 3% of any one issuer. Deposit notes and bank notes purchased through a broker or dealer shall be included with negotiable certificates of deposit in calculating allowable maximum percentages. Certificate of Deposit will be limited to maximum federally insured amount per issuer guaranteed by the Federal Deposit Insurance Corporation (FDIC).
10. Time Deposits. The City may invest in non-negotiable Certificates of Deposit at commercial banks and savings and loan associations that are collateralized in accordance with the California Government Code. To be eligible to receive City funds, the depository institution shall have received an overall rating of not less than "satisfactory" in its most recent evaluation of its record of meeting the credit needs of California's communities, including low and moderate-income neighborhoods. In selecting depositories, the credit worthiness of institutions shall be considered. Banks and savings and loan associations seeking to establish an investment relationship with the City shall submit an audited financial report that shall be reviewed for compliance with the City's investment standards. Any institution not providing an audited annual financial report shall be removed from the approved list and all funds maturing will be withdrawn. A list of eligible institutions shall be maintained. Qualification shall be determined by the following criteria:
  - a. Tangible capital must equal or exceed 1½%; core capital must equal or exceed 3%; and, risk-based capital must equal 8% of assets adjusted for assigned risk-weightings.
  - b. Return on assets of a minimum of a ½%; a return on equity of a minimum of 8%; an equity to assets ratio of a minimum of 5%; and, City investments shall be no greater than ½% of the total assets of the depository.
  - c. Independent auditor's statement must have a clean opinion.

11. Savings accounts. Savings accounts when used in conjunction with the City's checking accounts at a qualified bank where funds are collateralized in accordance with the California Government Code.
12. U. S. Government money market funds registered with the Securities and Exchange Commission and which comply with rule 2a7 of the Investment Company Act of 1940. The dollar weighted average maturity of the portfolio shall be less than ninety (90) days and the portfolio is managed to maintain a one dollar (\$1.00) share price. Also, the fund shall meet either of the following criteria: (a) Attained the highest ranking or the highest letter and numerical rating provided by not less than two Nationally Recognized Statistical-Rating Organizations; (b) retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience managing money market mutual funds with assets under management in excess of five hundred million dollars (\$500,000,000).
13. Repurchase Agreements. Investments in repurchase agreements or reverse repurchase agreements or securities lending agreements of any securities authorized by the Code, so long as the proceeds of the repurchase agreement are invested solely to supplement the income normally received from these securities. The City shall adopt as a standard the Bond Market Association Master Repurchase Agreement and shall maintain a list of approved counterparts and limit counter parties to primary dealers rated "A" or better by two Nationally Recognized Statistical-Rating Organizations. Reverse repurchase agreements and securities lending agreements shall require City Council authorization separate from City Council approval of this policy. Securities lending agreements shall include the following safeguard measures: terms of lending agreements, indemnification provisions, reinvestment guidelines, liquidity provisions, credit risks and monitoring requirements. Additionally any securities lending agreement shall be reviewed by the City Attorney to ensure the City's interests are properly protected.
  - a. Investments in repurchase agreements may be made, on any authorized investment, when the term of the agreement does not exceed one year.
  - b. Reverse repurchase agreements or securities lending agreements may be utilized when the security to be sold on the reverse repurchase agreement or securities lending agreement has been owned and fully paid for by the City for a minimum of thirty (30) days prior to sale; the total of all reverse repurchase agreements on investments owned by the City does not exceed 20% of the base value of the portfolio; and the agreement does not exceed a term of ninety two (92) days, unless the agreement includes a written codicil guaranteeing a minimum earning or spread for the entire period between sale of a security using a reverse repurchase agreement and the final maturity date of the same security.
14. Local Agency Investment Fund (LAIF). The City may invest in The Local Agency Investment Fund (LAIF), a special fund in the California State Treasury created and governed pursuant to Government Code Sections 16429.1 et seq. This law permits the City with the consent of the Board of Directors, to remit money not required for the City's immediate need, to the State City Treasurer for deposit in this special fund for the purpose of investment. LAIF currently limits investments to \$50 million from any one public agency by State law; therefore, there is a fifty million dollar (\$50,000,000) limit for the City of Pomona, fifty million dollar (\$50,000,000) limit for the Pomona Housing Authority, and a fifty million dollar (\$50,000,000) limit for the Pomona Public Financing Authority. The California Government Code states that monies placed for

deposit in LAIF are in trust in the custody of the State City Treasurer and cannot be borrowed or be withheld from the City. Further, the right of the City to withdraw its deposited money from the LAIF upon demand may not be altered, impaired, or denied in any way by any state official or agency based upon the State's failure to adopt a budget by July 1 of each new fiscal year.

15. Supranational. United States dollar-denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank, with a maximum remaining maturity of five years or less, and eligible for purchase and sale within the United States. Investments under this subdivision shall be rated in a rating category of "AA" or its equivalent or better by an NRSRO and shall not exceed 30 percent of the agency's moneys that may be invested in this section.

## **B. Collateralization**

Collateralization shall be required on two types of investments: Certificates of deposit and repurchase (and reverse repurchase) agreements. A collateral agreement must be current and on file before any funds can be transferred for collateralized certificates of deposit. Collateral shall be held by an independent third party with whom the City has a current written custodial agreement. A clearly marked evidence of ownership (safekeeping receipt) must be supplied to the City and retained. The right of collateral substitution is granted in accordance with the following requirements:

### **1. Certificates of Deposit**

- a. Government securities used as collateral require 102% of market value to the face amount of the deposit
- b. Promissory notes secured by first trust deeds used as collateral require 150% of market value to the face amount of the deposit
- c. Irrevocable letters of Credit issued by the Federal Home Loan Bank of San Francisco require 105% of market value to the face amount of the deposit

### **2. Repurchase and Reverse Repurchase Agreements**

- a. Only U.S. Treasury securities or federal agency securities are acceptable collateral. All securities underlying repurchase agreements must be delivered to the City's custodian bank versus payment or be handled under a properly executed tri-party repurchase agreement. The total market value of all collateral for each repurchase agreement must equal or exceed 102% of the total dollar value of the money invested by the City for the term of the investment. For any repurchase agreement with a term of more than one (1) day, the value of the underlying securities must be reviewed on an ongoing basis according to market conditions. Market value must be calculated each time there is a substitution of collateral.
- b. The City or its trustee shall have a perfected first security interest under the Uniform Commercial Code in all securities subject to a repurchase agreement.

### **C. Investments Not Approved**

Any security type or structure not specifically approved by this policy is hereby prohibited. Security types, which are hereby prohibited include, but are not limited to: Collateralized mortgage obligations (CMO's), mortgage pass-through securities, reverse repurchase agreements used as a leveraging vehicle, "exotic" derivatives structures such as range notes, dual index notes, inverse floating-rate notes, leveraged or de-leveraged floating-rate notes, interest-only strips that are derived from a pool of mortgages, any security that could result in zero interest accrual if held to maturity, any other complex variable or structured note with an unusually high degree of volatility or risk, purchasing or selling securities on margin, and the purchase of foreign currency denominated securities.

### **D. Exceptions to Prohibited and Restricted Investments**

The City shall not be required to sell securities prohibited or restricted in this policy, or any future policies, or prohibited or restricted by new State regulations, if purchased prior to their prohibition and/or restriction. Insofar as these securities provide no notable credit risk to the City, holding of these securities until maturity is approved. At maturity or liquidation, such monies shall be reinvested only as provided by this policy.

## **IX. INVESTING PARAMETERS**

### **A. Diversification**

The City shall diversify its investments by security type, issuer, maturity, and financial institutions. No percentage limitations are established for United States government, United States government agencies, United States government sponsored enterprises, and LAIF; however percentage limitations are established for other permitted investments, as noted in Section VII of this policy. The investments shall be diversified by limiting investments to avoid over-concentration in securities from a specific issuer or business sector (excluding U.S. Treasury, Federal Agency securities, and LAIF), limiting investment in securities that have higher credit risks, and investing in securities with varying maturities.

### **B. Maximum Maturities**

To the extent possible, the City will attempt to match its investments with anticipated cash flow requirements. Where there is no specified maturity limitation on an investment, no investment shall be made in any security, which, at the time of the investment, has a term remaining to maturity in excess of five (5) years, unless the City Council has granted express authority to make that investment no less than three months prior to the investment.

## **X. PORTFOLIO RISK MANAGEMENT**

### **A. Credit Risk**

Credit risk is the risk that a security or portfolio will lose some or all of its value due to a real or perceived change in the ability of the issuer to repay its debt. The City will mitigate credit risk by adoption the following strategies:

1. The diversification requirements included in Section IX are designed to mitigate credit risk in the portfolio
2. No more than 5% of the total portfolio may be invested in securities of any single issuer, other than the US Government, its agencies and enterprises

3. The City may elect to sell a security prior to its maturity and record a capital gain or loss in order to improve the quality, liquidity or yield of the portfolio in response to market conditions or City's risk preferences
4. If securities owned by the City are downgraded by either Moody's or S&P to a level below the quality required by this Investment Policy, it will be the City's policy to review the credit situation and make a determination as to whether to sell or retain such securities in the portfolio
  - a. If a security is downgraded, the City Treasurer, will use discretion in determining whether to sell or hold the security based on its current maturity, the economic outlook for the issuer, and other relevant factors
  - b. If a decision is made to retain a downgraded security in the portfolio, its presence in the portfolio will be monitored and reported monthly to the governing board.

## **B. Market Risk**

Market risk is the risk that the portfolio value will fluctuate due to changes in the general level of interest rates. The City recognizes that, over time, longer-term portfolios have the potential to achieve higher returns. On the other hand, longer-term portfolios have higher volatility of return. The City will mitigate market risk by providing adequate liquidity or short-term cash needs, and by making longer-term investments only with funds that are not needed for current cash flow purposes. The City further recognizes that certain types of securities, including variable rate securities, securities with principal paydowns prior to maturity, and securities with embedded options, will affect the market risk profile of the portfolio differently in different interest rate environments. The City, therefore, adopts the following strategies to control and mitigate its exposure to market risk:

1. The City will maintain a minimum of three months of budgeted operating expenditures in short term investments to provide sufficient liquidity or expected disbursements
2. The maximum percent of callable securities (does not include "make whole call" securities as defined in the Glossary) in the portfolio will be 20%
3. The maximum stated final maturity of individual securities in the portfolio will be five years, except as otherwise stated in this policy
4. The duration of the portfolio will at all times be approximately equal to the duration (typically plus or minus 20%) or Market Benchmark Index selected by the City based on the City's investment objectives, constraints and risk tolerances. The City's current Benchmark will be documented in the investment procedures manual.

## **XI. REPORTING**

The City Treasurer shall submit investment reports to the City Council that provide a clear picture of the status of the current investment portfolio and shall contain sufficient information to permit an independent organization to evaluate the performance of the investment program.

### **A. Reporting to City Council**

In accordance with California Government Code Section 53646, the City Treasurer shall submit to City Council, within thirty (30) days following the end of the quarter, an investment report that summarizes all securities in the portfolio. The report shall include:

1. Investment type
2. Purchase date

3. Maturity date
4. Credit quality
5. Coupon and yield
6. Book value
7. Market value
8. Interest Earnings
9. Average days to maturity
10. Statement of the ability to meet expenditures for the next six months (or an explanation as to why sufficient money shall, or may, not be available)

## **XII. PERFORMANCE STANDARDS**

The investment portfolio shall be managed in accordance with the parameters specified within this policy and always within consistently safe and prudent treasury management procedures.

### **A. Market Yield (Benchmark)**

The City's overall investment strategy is passive: Investments are generally held to maturity. If an investment advisory firm is retained by the City, the City portfolio shall be compared to a customized benchmark in order to determine whether market yields are being achieved. In addition, the quarter-to-date LAIF apportionment rate and the two-year U.S. Treasury Note shall also be considered useful benchmarks of the City's portfolio performance.

### **B. Marking to Market**

The market value of the portfolio shall be calculated at least quarterly. This will ensure that review of the investment portfolio, in terms of value and price volatility, has been performed. In defining market value, consideration shall be given to pronouncements from the Government Accounting Standards Board (GASB) that address the reporting of investment assets and investment income for all investment portfolios held by governmental entities. The fair value of all securities reported in the City's portfolio is based on currently quoted market prices.

## **XIII. INVESTMENT POLICY COMPLIANCE AND ADOPTION**

### **A. Policy Compliance and Changes**

Any deviation from the policy shall be reported to City Council at the next scheduled meeting. The City Treasurer shall promptly notify the City Council of any material change in the policy, and any modifications to the policy must be approved by the City Council.

### **B. Annual Statement of Investment Policy**

The City Treasurer shall render a written Investment Policy that shall be reviewed at least annually by the City Council to ensure its consistency with the overall objectives of preservation of principal, liquidity and return, and its relevance to current law and financial and economic trends. The City Council shall consider the annual Investment Policy and any changes therein at a public meeting. The Investment Policy shall be adopted by resolution of the City Council.

**C. Periodic Audit**

The City Treasurer will ensure as part of the City's annual audit treasury functions are reviewed and are in compliance with internal controls



## APPENDIX

### GLOSSARY OF INVESTMENT TERMS

**AGENCY:** A debt security issued by a federal or federally sponsored agency. Federal agencies are backed by the full faith and credit of the U.S. Government (i.e. Government National Mortgage Association). Federally sponsored agencies (FSA's) are backed by each particular agency with a market perception that there is an implicit government guarantee (i.e. Federal National Mortgage Association).

**ASKED PRICE:** The price at which securities are offered for sale, also known as offering price.

**BENCHMARK:** A comparative base for measuring the performance or risk tolerance of the investment portfolio. A benchmark should represent a close correlation to the level of risk and the average duration of the portfolio's investments.

**BID PRICE:** The price offered by a buyer of securities. (When you are selling securities, you *ask* for a bid.)

**BOND PROCEEDS:** The money paid to the issuer by the purchaser or underwriter of a new issue of municipal securities. These moneys are used to finance the project or purpose for which the securities were issued and to pay certain costs of issuance as may be provided in the bond contract.

**BOOK VALUE:** The value at which a debt security is shown on the holder's balance sheet. Book value is often acquisition cost plus/minus amortization and accretion, which may differ significantly from the security's current value in the market.

**BROKER:** Someone who brings buyers and sellers together and is compensated for his/her service.

**CERTIFICATE OF DEPOSIT (CD):** A time deposit with a specific maturity evidenced by a certificate. Large denomination CDs are typically negotiable.

**COLLATERAL:** Securities, evidence of deposit or other property which a borrower pledges to secure repayment of a loan. Also refers to securities pledged by a bank to secure deposits of public monies.

**COMMERCIAL PAPER:** The short-term unsecured debt of corporations.

**COUPON:** The rate of return at which interest is paid on a bond.

**CREDIT QUALITY:** The measurement of the financial strength of a bond issuer. This measurement helps an investor to understand an issuer's ability to make timely interest payments and repay the loan principal upon maturity. Generally, the higher the credit quality of a bond issuer, the lower the interest rate paid by the issuer because the risk of default is lower. Credit quality ratings are provided by a Nationally Recognized Statistical-Rating Organization.

**CREDIT RISK:** The risk to an investor that an issuer will default in the payment of interest and/or principal on a security.

**CUSTODIAN:** A bank or other financial institution that keeps custody of stock certificates and other assets.

**CURRENT YIELD (CURRENT RETURN):** A yield calculation determined by dividing the annual interest received on a security by the current market price of that security.

**DEALER:** A dealer, as opposed to a broker, acts as a principal in all transactions, by buying and selling for his/her own account.

**DELIVERY VERSUS PAYMENT:** There are two methods of delivery of securities: delivery versus payment and delivery versus receipt. Delivery versus payment is delivery of securities with an exchange of money for the securities. Delivery versus receipt is delivery of securities with an exchange of a signed receipt for the securities.

**DERIVATIVES:** (1) financial instruments whose return profile is linked to, or derived from, the movement of one or more underlying index or security, and may include a leveraging factor, or (2) financial contracts based upon notional amounts whose value is derived from an underlying index or security (interest rates, foreign exchange rates, equities or commodities).

**DISCOUNT:** The difference between the par value of a bond and the cost of the bond, when the cost is below par. Some short-term securities, such as T-bills and banker's acceptances, are known as discount securities. They sell at a discount from par, and return the par value to the investor at maturity without any additional interest. Other securities, which have fixed coupons, trade at a discount when the coupon rate is lower than the current market rate for securities of that maturity and/or quality.

**DIVERSIFICATION:** Dividing investment funds among a variety of security types by sector, maturity and quality ratings offering independent returns.

**DURATION:** A measure of the timing of the cash flows, such as the interest payments and the principal repayment, to be received from a given fixed-income security. This calculation is based on three variables: term to maturity, coupon rate, and yield to maturity. The duration of a security is a useful indicator of its price volatility for given changes in interest rates.

**FAIR VALUE:** The amount at which an investment could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

**FEDERAL CREDIT AGENCIES:** Agencies of the Federal Government set up to supply credit to various classes of institutions and individuals, e.g., S&L's, small-business firms, students, farmers, farm co-operatives, and exporters.

**FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC):** A federal agency that insures bank deposits currently up to \$250,000 per deposit.

**FEDERAL HOME LOAN BANKS (FHLB):** Government sponsored wholesale banks (currently 12 regional banks) that lend funds and provide correspondent banks services to member commercial banks, thrift institutions, credit unions and insurance companies.

**FEDERAL NATIONAL MORTGAGE ASSOCIATION (FNMA):** FNMA is a federal corporation working under the auspices of the Department of Housing and Urban Development (HUD). It is the largest single provider of residential mortgage funds in the United States. Fannie Mae, as the corporation is called, is a private stockholder-owned corporation. The corporation's purchases include a variety of adjustable mortgages and second loans, in addition to fixed-rate mortgages.

**FEDERAL OPEN MARKET COMMITTEE (FOMC):** Consists of seven members of the Federal Reserve Board and five of the twelve Federal Reserve Bank Presidents. The President of the New York Federal Reserve Bank is a permanent member, while the other Presidents serve on a rotating basis. The Committee periodically meets to set Federal Reserve guidelines regarding purchases and sales of Government Securities in the open market as a means of influencing the volume of bank credit and money.

**FEDERAL RESERVE SYSTEM:** The central bank of the United States created by Congress and consisting of a seven member Board of Governors in Washington, D.C., twelve Regional Banks and about 5,700 commercial banks that are members of the system.

**FINANCIAL INDUSTRY REGULATORY AUTHORITY (FINRA):** A self-regulatory organization (SRO) responsible for governing business between brokers, dealers and the investing public.

**GOVERNMENT ACCOUNTING STANDARDS BOARD (GASB):** A standard-setting body, associated with the Financial Accounting Foundation, which prescribes standard accounting practices for governmental units.

**GOVERNMENT NATIONAL MORTGAGE ASSOCIATION (GNMA or Ginnie Mae):** Securities influencing the volume of bank credit guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loan associations, and other institutions. Security holder is protected by full faith and credit of the U.S.

Government. Ginnie Mae securities are backed by the FHA, VA, or FMHA mortgages. The term “pass-throughs” is often used to describe Ginnie Maes.

**GOVERNMENT SECURITIES:** An obligation of the U.S. government, backed by the full faith and credit of the government. These securities are regarded as the highest quality of investment securities available in the U.S. securities market. See "Treasury Bills, Notes, and Bonds."

**INTEREST RATE RISK:** The risk associated with declines or rises in interest rates which cause an investment in a fixed-income security to increase or decrease in value.

**INTERNAL CONTROLS:** An internal control structure designed to ensure that the assets of the entity are protected from loss, theft, or misuse. The internal control structure is designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that 1) the cost of a control should not exceed the benefits likely to be derived and 2) the valuation of costs and benefits requires estimates and judgments by management. Internal controls should address the following points:

- **CONTROL OF COLLUSION** – Collusion is a situation where two or more employees are working in conjunction to defraud their employer.
- **Separation of transaction authority from accounting and record keeping** – By separating the person who authorizes or performs the transaction from the people who record or otherwise account for the transaction, a separation of duties is achieved.
- **Custodial safekeeping** – Securities purchased from any bank or dealer including appropriate collateral (as defined by state law) shall be placed with an independent third party for custodial safekeeping.
- **Avoidance of physical delivery securities** – Book-entry securities are much easier to transfer and account for since actual delivery of a document never takes place. Delivered securities must be properly safeguarded against loss or destruction. The potential for fraud and loss increases with physically delivered securities.
- **Clear delegation of authority to subordinate staff members** – Subordinate staff members must have a clear understanding of their authority and responsibilities to avoid improper actions. Clear delegation of authority also preserves the internal control structure that is contingent on the various staff positions and their respective responsibilities.
- **Written confirmation of transactions for investments and wire transfers** – Due to the potential for error and improprieties arising from telephone and electronic transactions, all transactions should be supported by written communications and approved by the appropriate person. Written communications may be via fax if on letterhead and if the safekeeping institution has a list of authorized signatures.
- **Development of a wire transfer agreement with the lead bank and third-party custodian** – The designated official should ensure that an agreement will be entered into and will address the following points: controls, security provisions, and responsibilities of each party making and receiving wire transfers.

**LIQUIDITY:** A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value. In the money market, a security is said to be liquid if the spread between bid and asked prices is narrow and reasonable size can be done at those quotes.

**LOCAL AGENCY INVESTMENT FUND (LAIF):** Chapter 730, Statutes of 1976 of the State of California, established the Local Agency Investment Fund. This fund enables local governmental agencies to remit money not required for immediate needs to the State City Treasurer for the purpose of investment. In order to derive the maximum rate of return possible, the State City Treasurer has elected to invest these monies with State monies as a part of the Pooled Money Investment Account. Each local governmental unit has the exclusive determination of the length of time its money will be on deposit with the State City Treasurer. At

the end of each calendar quarter, all earnings derived from investments are distributed by the State Controller to the participating government agencies in proportion to each agency's respective amounts deposited in the Fund and the length of time such amounts remained therein. Prior to the distribution, the State's costs of administering the program are deducted from the earnings.

**MAKE WHOLE CALL:** A type of call provision on a bond that allows the issuer to pay off the remaining debt early. Unlike a call option, with a make whole call provision, the issuer makes a lump sum payment that equals the net present value (NPV) of future coupon payments that will not be paid because of the call. With this type of call, an investor is compensated, or "made whole."

**MARK-TO-MARKET:** The process whereby the book value or collateral value of a security is adjusted to reflect its current market value.

**MARKET RISK:** The risk that the value of a security will raise or decline as a result of changes in market conditions.

**MARKET VALUE:** The current price at which a security is trading and could presumably be purchased or sold at that particular point in time.

**MASTER REPURCHASE AGREEMENT:** A written contract covering all future transactions between the parties to repurchase-reverse repurchase agreements that establish each party's rights in the transactions. A master agreement will often specify, among other things, the right of the buyer-lender to liquidate the underlying securities in the event of default by the seller-borrower.

**MATURITY:** The date upon which the principal or stated value of a financial obligation is due and payable.

**MONEY MARKET:** The market in which short term debt instruments (T-bills, discount notes, commercial paper and banker's acceptances) are issued and traded.

**MONEY MARKET MUTUAL FUND:** Mutual funds that invest solely in money market instruments (short-term debt instruments, such as Treasury bills, commercial paper, bankers' acceptances, repos and federal funds).

**MUTUAL FUND:** An investment company that pools money and can invest in a variety of securities, including fixed-income securities and money market instruments. Mutual funds are regulated by the Investment Company Act of 1940 and must abide by Securities and Exchange Commission (SEC) disclosure guidelines.

**NATIONALLY RECOGNIZED STATISTICAL-RATING ORGANIZATION (NRSRO):** Standard and Poor's, Moody's, and Fitch Financial Services are examples of such organizations.

**OFFER:** An indicated price at which market participants are willing to sell a security or commodity. Also referred to as the "Ask price."

**PAR VALUE:** The amount of principal that must be paid at maturity. Also referred to as the face amount of a bond, normally quoted in \$1,000 increments per bond.

**PORTFOLIO:** Combined holding of more than one stock, bond, commodity, real estate investment, cash equivalent, or other asset. The purpose of a portfolio is to reduce risk by diversification.

**PREMIUM:** The difference between the par value of a bond and the cost of the bond, when the cost is above par.

**PRINCIPAL:** The face value or par value of a debt instrument, or the amount of capital invested in a given security.

**PRIMARY DEALER:** A group of government securities dealers who submit daily reports of market activity and monthly financial statements to the Federal Reserve Bank of New York and are subject to its informal oversight. Primary dealers include Securities and Exchange Commission (SEC) registered securities broker/dealers, banks and a few unregulated firms.

**PRINCIPAL:** (1) The face amount or par value of a debt instrument. (2) One who acts as a dealer buying and selling for his own account.

**PRUDENT PERSON (MAN) Rule:** A standard of responsibility which applies to fiduciaries. In California, the rule is stated as "Investments shall be managed with care, skill, prudence and diligence, under the circumstances then prevailing, that a prudent person, acting in a like capacity and familiar with such matters, would use in the conduct of an enterprise of like character and with like aims to accomplish similar purposes."

**RATE OF RETURN:** The yield obtainable on a security based on its purchase price or its current market price. This may be the amortized yield to maturity on a bond or the current income return.

**REALIZED YIELD:** The change in value of the portfolio due to interest received, interest earned, realized gains and losses. It does not give effect to changes in market value on securities, which have not been sold from the portfolio.

**REINVESTMENT RISK:** The risk that a fixed-income investor will be unable to reinvest income proceeds from a security holding at the same rate of return currently generated by that holding.

**REPURCHASE AGREEMENT (RP OR REPO):** A holder of securities sells these securities to an investor with an agreement to repurchase them at a fixed price on a fixed date. The security "buyer" in effect lends the "seller" money for the period of the agreement, and the terms of the agreement are structured to compensate the buyer for this. Dealers use RP extensively to finance their positions. Exception: When the Fed is said to be doing RP, it is lending money that is increasing bank reserves.

**REVERSE REPURCHASE AGREEMENT:** An agreement of one party (for example, a financial institution) to purchase securities at a specified price from a second party (such as a public agency) and a simultaneous agreement by the first party to resell the securities at a specified price to the second party on demand or at a specific date.

**RISK:** Degree of uncertainty of return on an asset.

**RULE 2A-7 OF THE INVESTMENT COMPANY ACT:** Applies to all money market mutual funds and mandates such funds to maintain certain standards, including a 13-month maturity limit and a 90-day average maturity on investments, to help maintain a constant net asset value of one dollar (\$1.00).

**SAFEKEEPING SERVICE:** A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank's vault for protection and security.

**SECONDARY MARKET:** A market is made for the purchase and sale of outstanding issues following the initial distribution.

**SECURITIES LENDING:** An agreement under which a local agency agrees to transfer securities to a borrower who, in turn, agrees to provide collateral to the local agency. During the term of the agreement, both the securities and the collateral are held by a third party. At the conclusion of the agreement, the securities are transferred back to the local agency in return for the collateral.

**SHORT TERM:** Less than one (1) years' time.

**SPREAD:** The difference between coupon rate and U.S. Treasury Obligations Interest benchmark

**STRUCTURED NOTES:** Notes issued by Government Sponsored Enterprises, (FHLB, FNMA, FHLMC, etc.), and Corporations that have imbedded options, (e.g., call features, step-up coupons, floating rate coupons, derivative-based returns), into their debt structure. Their market performance is impacted by the fluctuation of interest rates, the volatility of the imbedded options and shifts in the shape of the yield curve.

**SWAP:** Trading one asset for another.

**TOTAL RATE OF RETURN:** A measure of a portfolio's performance over time. It is the internal rate of return, which equates the beginning value of the portfolio with the ending value; it includes interest earning, realized and unrealized gains, and losses in the portfolio.

**U.S. TREASURY OBLIGATIONS:** Securities issued by the U.S. Treasury and backed by the full faith and credit of the United States. Treasuries are considered to have no credit risk, and are the benchmark for interest rates on all other securities in the US and overseas. The Treasury issues both discounted securities and fixed coupon notes and bonds.

**TREASURY BILLS:** Short-term U.S. government non-interest bearing discounted debt securities with maturities of no longer than one year and issued in minimum denominations of \$10,000. Auctions of three- and six-month bills are weekly, while auctions of one-year bills are monthly. The yields on these bills are monitored closely in the money markets for signs of interest rate trends.

**TREASURY BOND:** A long-term coupon-bearing U.S. Treasury security issued as a direct obligation of the U.S. Government and having an initial maturity of more than 10 years and issued in minimum denominations of \$1,000.

**TREASURY NOTE:** A medium-term coupon-bearing U.S. Treasury security issued as a direct obligation of the U.S. Government and having an initial maturity of from one to ten years and issued in denominations ranging from \$1,000 to \$1 million or more.

**UNIFORM NET CAPITAL RULE:** Securities and Exchange Commission (SEC) Rule 15C3-1 outlining requirements that member firms as well as nonmember broker-dealers in securities maintain a maximum ratio of indebtedness to liquid capital of 15 to 1; also called net capital rule and net capital ratio. Indebtedness covers all money owed to a firm, including margin and commitments to purchase securities, one reason new public issues are spread among members of underwriting syndicates. Liquid capital includes cash and assets easily converted into cash.

**VOLATILITY:** A degree of fluctuation in the price and valuation of securities.

**YIELD:** The current rate of return on an investment security generally expressed as a percentage of the security's current price. (a) **INCOME YIELD** is obtained by dividing the current dollar income by the current market price for the security. (b) **NET YIELD** or **YIELD TO MATURITY** is the current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond.