

**The City of Mission Viejo**  
**Investment Policy**  
Fiscal Year 2018-19

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## I. Investment Philosophy

### A. Policy

1. This Investment Policy is set forth by the City of Mission Viejo (the "City") for the following purposes:
  - a. To establish a clear understanding for the City Council of the City (the "City Council"), the Investment Advisory Commission (IAC), City management, responsible employees, citizens and third parties of the objectives, policies and guidelines for the investment of the City's idle and surplus funds.
  - b. To offer guidance to investment staff and any external investment advisers on the investment of the City funds.
  - c. To establish a basis for evaluating investment results.
2. The City establishes investment policies which meet its current investment goals. The City shall review this policy annually, and may change its policies more frequently as its investment objectives change.

### B. Objectives

The objectives of this investment policy are, in order of priority:

1. To ensure the safety of invested funds in compliance with all Federal, State and local laws governing the investment of moneys under the control of the City Treasurer.
2. To maintain sufficient liquidity to meet cash flow needs.
3. To attain a "market average rate of return" consistent with the primary objectives of safety and liquidity. The expected rate of return on the City's portfolio is more specifically defined in Section IV.

### C. Prudence

1. The Prudent Investor Standard shall be used by investment officials, and shall be applied in the context of managing an overall portfolio. Investment staff 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 within 30 days and appropriate

action is taken to control adverse developments.

2. The “Prudent Investor Standard:” Governing bodies of local agencies or persons authorized to make investment decisions on behalf of those local agencies investing public funds pursuant to this chapter are trustees and therefore fiduciaries subject to the prudent investor standard. When investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, that a prudent investor acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency. Within the limitations of the foregoing Prudent Investor Standard and considering individual investments as part to an overall strategy, a trustee is authorized to acquire investments as authorized by law, except as prohibited in this investment policy.

D. Ethics and Conflicts of Interest

State law, City statutes and City personnel and purchasing policies shall be followed to avoid conflict of interest or the appearance thereof. In addition to the applicable requirements of the Political Reform Act and Government Code Section 1090, the City Treasurer, Administrative Services Manager – Treasury, and City Manager, members of the City Council, members of the Investment Advisory Commission, their spouses and investment consultants shall refrain from personal business activity that could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions on behalf of the City. In addition, these individuals shall disclose to the City Manager any financial interests in or financial relationships with financial institutions that conduct business with the City, and shall subordinate their personal investment transactions to those of the City’s, particularly with regard to the timing of purchases and sales. Unless otherwise prohibited by State law, City statutes, policies or regulations, it is permissible for the City to purchase securities from firms in which members of the Investment Advisory Commission are officers, partners, members, or employees, provided that: (1) multiple bids are obtained for such purchases; (2) the affected member abstains from participation in the recommendation of the Investment Advisory Commission as to the firm with which the member has an employment or ownership relationship; (3) the member’s relationship to the securities firm is stated in the minutes of the Investment Advisory Commission; and (4) the affected member of the Investment Advisory Commission does not participate in the sale of securities to the City as an officer, partner, member, or employee of the securities firm; and (5) the firm meets the requirements of Section II. C. of this Investment Policy.

All bond issue providers including but not limited to underwriters, bond counsel, financial advisors, brokers and dealers, will disclose any fee sharing arrangements or fee splitting to the City Manager prior to the execution of any transactions. The providers must disclose the percentage share and approximate dollar amount share to the City prior to the execution of any transactions.

## II. Operational and Procedural matters

### A. Scope

This investment policy applies to all financial assets and investment activities of the City except for proceeds of debt issuance. Debt proceeds shall be invested in accordance with the investment objectives of the City as set forth in this policy; however, such proceeds are invested in accordance with permitted investment provisions of their specific bond indentures. All deviations from investments authorized in this policy for other City funds shall be disclosed to the City Council at the time bond documents are considered for approval. Proceeds of debt issuance shall be subject to the operational and reporting requirements of this policy.

### B. Delegation of Authority

1. Authority to manage the City's investment program is derived from the California Government Code Sections 53600 *et seq.*
2. The City Treasurer will be responsible for the overall management of the investment program and the Administrative Services Manager - Treasury will be responsible for carrying out the day-to-day activities. The City of Mission Viejo Municipal Code, Chapter 3.08, authorizes the City Treasurer to invest funds in accordance with California Government Code Section 53600 *et seq.* The Treasurer shall be responsible for all transactions undertaken by the City's internal staff, and shall establish a system of controls to regulate the activities of internal staff and external investment advisers engaged in accordance with Section II B (5).
3. In the absence of the City Treasurer, the investment responsibilities are hereby delegated to the Administrative Services Manager - Treasury.
4. In the absence of both the City Treasurer and the Administrative Services Manager - Treasury, the City Manager has that responsibility.
5. The City Council may, upon recommendation of the Investment Advisory Commission, 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 limited 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, or be exempt from such registration. Such external managers shall be prohibited from 1) executing safekeeping arrangements, and 2) executing wire transfers. This Section does not preclude the City Treasurer from retaining portfolio consultants within existing authority.

C. Authorized Financial Dealers and Institutions

1. The Treasurer will maintain a list of financial institutions authorized to provide investment services to the City. Institutions eligible to transact investment business with the City include:
  - a. Primary government dealers as designated by the Federal Reserve Bank and non-primary government dealers,
  - b. Nationally or state-chartered banks,
  - c. The Federal Reserve Bank, and
  - d. Direct issuers of securities eligible for purchase by the City.
2. Selection of financial institutions and broker/dealers authorized to engage in transactions with the City shall be at the sole discretion of the City, except where the Agency utilizes an external investment manager in which case the City may rely on the investment manager for selection.
3. The Treasurer and the IAC shall obtain information from qualified financial institutions to determine if the institution makes markets in securities appropriate for the City's needs, can assign qualified sales representatives and can provide written agreements to abide by the conditions set forth in the City of Mission Viejo Investment Policy. Investment accounts with all financial institutions shall be standard non-discretionary accounts and may not be margin accounts.
4. All financial institutions which desire to become qualified bidders for investment transactions must supply the Treasurer with the following:
  - a. Audited financial statements for the institution's three most recent fiscal years.
  - b. At least three references from California local agencies

whose portfolio size, investment objectives and risk preferences are similar to the City's.

c. A statement certifying that the institution has reviewed the California Government Code Section 53600 *et seq.* and the City's Investment Policy and that all securities offered to the City shall comply fully and in every instance with all provisions of the California Government Code.

5. The signatures of two individuals shall be required for the opening and closing of any bank account and broker account (the Treasurer or City Manager, and the Mayor or Mayor Pro Tem). The Administrative Services Manager - Accounting, who is independent of the investment function, shall keep a record of all opened and closed accounts. On an annual basis, the Administrative Services Manager - Accounting shall provide this list of accounts to the City's independent auditor.

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

7. Whenever possible, transactions with broker/dealers shall be selected on a competitive basis and their bid or offering prices shall be recorded. If there is no other readily available competitive offering, best efforts will be made to document quotations for comparable or alternative securities. When purchasing original issue instrumentality securities, no competitive offerings will be required as all dealers in the selling group offer those securities at the same original issue price.

D. Delivery vs. payment

All investment transactions of the City shall be conducted using standard delivery-vs.-payment procedures.

E. Safekeeping of securities

To protect against potential losses by collapse of individual securities dealers, and to enhance access to securities, interest payments and maturity proceeds, all securities owned by the City shall be held in safekeeping by a third party bank trust department, acting as agent for the City under the terms of a custody agreement executed by the bank and by the City. The only exception to the foregoing shall be securities purchases made with: (1) local government investment pools, (2) direct purchases of local agency obligations as described in section III.A.12(a)(ii) of this

investment policy; and (3) money market mutual funds, since these securities are not deliverable.

From time to time, the City may invest funds received late in the day in one to thirty day repurchase agreements with its depository bank. Securities used as collateral for such repurchase agreements may be held in safekeeping by the City's depository bank.

Investments are to be held in the City's name in conjunction with industry standards, including collateral held for repurchase agreements by depository banks.

### III. Permitted investments and portfolio risk management

#### A. Investments authorized for purchase by City staff

All investments shall be made in accordance with Sections 53600 *et seq.* of the Government Code of California and as described within this Investment Policy. Limits identified are to be based on the "market value" of the investment. Where this section does not specify a limitation on the term or remaining maturity at the time of the investment, no investment shall be made in any investment that at the time of the investment has a term remaining to maturity in excess of five years, unless the legislative body has granted express authority to make that investment either specifically or as part of an investment program approved by the legislative body no less than three months prior to the investment. Permitted investments under this policy shall include:

1. Securities issued by the U.S. Treasuries and other government obligations for which the full faith and credit of the United States are pledged for the payment of principal and interest. There shall be no maximum allowable investment in U.S. Treasuries provided that the maximum maturity is five (5) years.
2. Securities issued and backed as to payment by one of the following Government Sponsored Entities (GSE's): the Federal Farm Credit Bank, Federal Home Loan Bank, Federal Home Loan Mortgage Corporation, and the Federal National Mortgage Association, provided that:
  - a. No more than 25% of the portfolio be invested in securities issued by any single agency.
  - b. Only senior debt is permitted; purchase of subordinated debt is prohibited.
  - c. The maximum maturity does not exceed five (5) years.

3. Banker's acceptances provided that:
  - a. They are issued by institutions which have short-term debt obligations of which are rated a minimum of "A-1" or higher, or equivalent, by at least one nationally recognized statistical rating organization ("NRSRO"); Or long-term debt obligations which are rated in a rating category of "A" or higher, or equivalent by at least one NRSRO.
  - b. The acceptance is eligible for purchase by the Federal Reserve System.
  - c. The maturity does not exceed 180 days.
  - d. No more than 40% of the total portfolio may be invested in banker's acceptances, and
  - e. No more than 5% of the portfolio may be invested in any single issuer.
4. Federally insured time deposits (Non-negotiable certificates of deposit) in state or federally chartered banks, savings and loans, or credit unions, provided that:
  - a. The amount per institution is limited to the maximum covered under federal insurance.
  - b. No more than 20% of the portfolio will be invested in a combination of federally insured and collateralized time deposits.
  - c. The maximum maturity does not exceed five (5) years.
5. Collateralized time deposits (Non-negotiable certificates of deposit), in state or federally chartered banks, savings and loans, or credit unions in excess of insured amounts which are fully collateralized with securities in accordance with California law, provided that:
  - a. No more than 20% of the portfolio shall be invested in a combination of federally insured and collateralized time deposits, and
  - b. The federally insured and/or collateralized time deposits are issued by institutions which have long-term debt rated "A", "A-1" for short-term, their equivalent, or better by at least one NRSRO.

- c. The maturity of such deposits does not exceed five (5) years.
  - d. Any commercial bank or savings and loan association shall deposit eligible securities with an agency of a depository approved by the State Banking Department to secure any uninsured portion of a Non-Negotiable Certificate of Deposit. The value of eligible securities as defined pursuant to California Government Code, Section 53651, pledged against a Certificate of Deposit shall be equal to 150% of the face value of the CD if the securities are classified as mortgages and 110% of the face value of the CD for all other classes of security.
6. Negotiable certificates of deposit (NCDs), issued by a nationally or state-chartered bank, a savings association or a federal association, a state or federal credit union, or by a federally licensed or state-licensed branch of a foreign bank, provided that:
- a. The amount of the NCD insured up to the FDIC limit does not require any credit ratings.
  - b. Any amount above the FDIC insured limit must be issued by institutions which have short-term debt obligations rated “A-1” or its equivalent or better by at least one NRSRO; or long-term debt obligations rated in a rating category of “A”, or its equivalent, or better by at least one NRSRO.
  - c. The maximum maturity does not exceed five (5) years.
  - d. No more than 30% of the total portfolio may be invested in NCDs (combined with CDARS).
  - e. No more than 5% of the portfolio may be invested in any single issuer.
7. Certificate of Deposit Placement Service (CDARS), provided that:
- a. No more than 30% of the total portfolio may be invested in combination of Certificates of Deposit, including CDARS.
  - b. The maximum maturity does not exceed five (5) years.
8. Collateralized Bank Deposits. This is the process by which a bank or financial institution pledges securities, or other deposits for the purpose of securing repayment of deposited funds. The City’s deposits with financial institutions will be collateralized with pledge securities per California Government Code, Section 53651.

9. Repurchase agreements collateralized with securities authorized under California Government Code, maintained at a level of at least 102% of the market value of the Repurchase Agreements. There are no limits on the dollar amount or percentage that the City may invest, provided that:
  - a. The maximum maturity does not exceed one (1) year.
  - b. Securities used as collateral for Repurchase Agreements will be delivered to an acceptable third party custodian.
  - c. The repurchase agreements are the subject to a Master Repurchase Agreement between the City and the provider of the repurchase agreement. The Master Repurchase Agreement shall be substantially in the form developed by the Securities Industry and Financial Markets Association (SIFMA).
  - d. The securities which collateralize the repurchase agreement shall be priced at Market Value, including any accrued interest plus a margin. The Market Value of the securities that underlie a repurchase agreement shall be valued at 102% or greater of the funds borrowed against those securities.
  - e. Financial institutions shall mark the value of the collateral to market at least monthly and increase or decrease the collateral to satisfy the ratio requirement described above.
  - f. The City shall receive monthly statements of collateral.
  
10. Commercial paper provided that
  - a. The maturity does not exceed 270 days from the date of purchase.
  - b. The issuer is a corporation organized and operating in the United States with assets in excess of \$500 million.
  - c. The securities are rated "A-1" or higher, or equivalent, by at least one NRSRO.
  - d. They are issued by corporations which have long-term obligations rated in a rating category of "A" or higher, or equivalent, by at least one NRSRO

- e. The City may purchase no more than 10% of the outstanding commercial paper of any single issuer.
  - f. No more than 25% of the portfolio is invested in commercial paper.
  - g. No more than 5% of the portfolio may be invested in any single issuer.
11. State of California Local Agency Investment Fund (“LAIF”), provided that:
- a. The maximum amount permitted by the State of California.
  - b. LAIF investments in instruments prohibited by or not specified in the City's policy do not exclude it from the City's list of allowable investments, provided that the fund's reports allow the Treasurer to adequately judge the risk inherent in LAIF's portfolio, and provided that disclosure of such investments, if any, is made annually to the City Council.
12. Orange County Investment Pool (“OCIP”), provided that:
- a. No more than 10% of the total portfolio shall be invested in the OCIP.
  - b. OCIP investments in instruments prohibited by or not specified in the City's policy do not exclude it from the City's list of allowable investments, provided that the fund's reports allow the Treasurer to adequately judge the risk inherent in OCIP's portfolio, and provided that disclosure of such investments, if any, is made annually to the City Council.
13. Local agency sponsored investment pools specifically approved for investment by the City Council upon recommendation of the IAC, provided that:
- a. All pool investments must be permitted under California Government Code Section 53601 *et seq.*
  - b. The pool shall have achieved a rating of “Aaa” by a NRSRO, or shall be insured by a municipal insurance corporation.
  - c. The pool marks its portfolio to market at least weekly.
  - d. The pool provides comprehensive, timely monthly reports which include detailed transaction listings; reports realized

and unrealized gains and losses, provides accurate market values for each security, provides a quality rating for all investment securities, takes delivery of all securities prior to payment, provides for third party safekeeping of all investments, and for whom an audit is conducted annually by an independent auditor other than the local agency's internal auditors.

- e. No more than 15% of the total portfolio shall be invested in such pools.
- f. The City's investment in any pool shall comprise no more than 5% of the market value of the total assets of the investment pool, measured at month end.
- g. Pool investments in instruments prohibited by or not specified in the City's policy do not exclude it from the City's list of allowable investments, provided that the Pool's reports allow the Treasurer to adequately judge the risk inherent in the Pool's portfolio, and provided that disclosure of such investments is made prior to any investment in such Pool, and annually to the City Council.

14. Mutual funds and Money Market Mutual Funds invested in US government securities permitted under this policy and under the California Government Code Section 53601 with final stated maturities of one year or less ("Government money market funds"). In order to be eligible for investment under this section, one investment objective of such a fund must be to maintain a price of \$1.00 per share. The following criteria must also be met:

- a. The fund shall be registered with the Securities and Exchange Commission, and have attained the highest ranking or the highest letter and numerical rating provided by not less than two (2) NRSROs; or
- b. Have 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 \$500 million.
- c. No more than 10% of the portfolio may be invested in any one fund.
- d. Investment in such funds shall not exceed 20% of the City's total portfolio.

- e. Investments in instruments prohibited by or not specified in the City's policy do not exclude it from the City's list of allowable investments, provided that the fund's reports allow the Treasurer to adequately judge the risk inherent in the fund's portfolio, and provided that disclosure of such investments is made prior to any investment in such fund and annually to the City Council.
15. MUNICIPAL SECURITIES, including bonds, notes, warrants, or other evidences of indebtedness or obligations of the State of California, the City, or any other local agency within the State of California (as to which may include obligations payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the local agency, or by a department, board, agency, or authority of the local agency); provided that:
- a. (i) The securities are rated "A" or its equivalent or higher by at least one NRSRO, or (ii) if the Local Agency securities are unrated, such securities (A) are directly purchased by the City from the Local Agency, as issuer thereof, and made payable to the City with restrictions prohibiting transfer thereof, (B) the local agency issuing the securities is located within the jurisdiction of the City, and (C) the City Council of the City, prior to acquisition of such securities, makes a finding that such acquisition is in the furtherance of a project providing a public benefit to the City.
  - b. No more than 5% of the portfolio may be invested in any single issuer; provided that, with respect to investments described in subparagraph 15(a)(ii) above, no more than \$5 million of the portfolio may be invested in any single issuer.
  - c. No more than 30% of the portfolio may be in Municipal Securities.
  - d. The maximum maturity does not exceed five (5) years, except in the case of securities found to be of public benefit to the City as provided in section 15(a)(ii)(C) above, in which case the maximum maturity does not exceed twenty (20) years.
16. Municipal Securities (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 a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of any of the other 49 states, in addition to California, provided that:

- a. The securities are rated in a rating category of “A” or its equivalent or higher by at least one NRSRO.
- b. No more than 5% of the portfolio may be invested in any single issuer.
- c. No more than 30% of the portfolio may be in Municipal Securities.
- d. The maximum maturity does not exceed five (5) years.

17. SUPRANATIONALS, provided that:

- a. Issues are US 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.
- b. The securities are rated “AA” or its equivalent or better by at least one NRSRO.
- c. No more than 30% of the portfolio may be invested in these securities.
- d. No more than 10% of the portfolio may be invested in any single issuer.
- e. The maximum maturity does not exceed five (5) years.

18. Corporate Medium Term Notes (MTNs), provided that:

- a. The issuer is a corporation 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.
- b. The securities are rated in a rating category of “A” or its equivalent or better by at least one NRSRO
- c. No more than 30% of the total portfolio may be invested in MTNs.
- d. No more than 5% of the portfolio may be invested in any single issuer.

- e. The maximum maturity does not exceed five (5) years.
19. Asset-Backed, Mortgage-Backed, Mortgage Pass-Through Securities, and Collateralized Mortgage Obligations, provided that:
- a. The securities are rated in a rating category of “AA” or its equivalent or higher by a NRSRO.
  - b. They are issued by an issuer having long-term debt obligations rated in a rating category of “A” or its equivalent or higher by at least one NRSRO.
  - c. No more than 20% of the total portfolio may be invested in these securities.
  - d. No more than 5% of the portfolio may be invested in any single Asset-Backed or Commercial Mortgage security issuer. There is no issuer limitation on any Mortgage security where the issuer is the US Treasury or a Federal Agency/GSE.
  - e. The maximum legal final maturity does not exceed five (5) years.

B. Prohibited investment vehicles and practices

- 1. State law notwithstanding, any investments not specifically described herein including, but not limited to, mutual funds, other than government money market funds as described in Section III A (14), unregulated and/or unrated investment pools or trusts, except as specified above, futures and options, inverse floaters, range notes, mortgage derived interest only-strips, variable rate securities and securities with embedded options.
- 2. Investment in any security that could result in a zero interest accrual if held to maturity is prohibited.
- 3. Trading securities for the sole purpose of speculating on the future direction of interest rates is prohibited.
- 4. Purchasing or selling securities on margin is prohibited.
- 5. The use of reverse repurchase agreements, securities lending or any other form of borrowing or leverage is prohibited.
- 6. Borrowing for investment purposes is prohibited.
- 7. The purchase of foreign currency denominated securities is

prohibited.

C. Investments and practices permitted for use by external investment managers.

1. Professional investment managers that may be retained by the City may request more latitude in their choice of investment vehicles and practices than is allowed under this policy. As an integral part of their service to the City, such advisers shall recommend additional investment vehicles and practices, with limitations and restrictions on their use. The City Council must approve the investment vehicles and practices, upon the recommendation of the IAC, and adopt an appropriate amendment to this policy prior to their implementation.

D. Mitigating credit risk in the portfolio

Credit risk is the risk that a security or a 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 shall mitigate credit risk by adopting the following strategies:

1. The diversification requirements included in Section III (A) 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, unless otherwise specified in this policy. Limits are to be based on the "market value" of the investment.
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 the City's risk preferences.
4. If securities owned by the City are downgraded by a NRSRO to a level below the quality required by this Investment Policy, it shall 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 Treasurer will use discretion in determining whether to sell or hold the security based on its current maturity, the loss in value, 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 City Manager and City Council.

E. Mitigating market risk in the portfolio

Market risk is the risk that the portfolio will decline in value (or will not optimize its value) due to changes in the general level of interest rates. The City recognizes that, over time, longer-term portfolios achieve higher returns. On the other hand, longer-term portfolios have higher volatility of return. The City shall mitigate market risk by providing adequate liquidity for short-term cash needs, and by making some longer-term investments only with funds which are not needed for cash flow purposes. The City further recognizes that certain types of securities, including variable rate securities, securities with principal pay downs 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 maximum stated final maturity of individual securities in the portfolio shall be five years, except as otherwise stated in this policy.
2. The City shall maintain a minimum of six months of budgeted operating and capital expenditures (excluding expenditures financed with bond proceeds) in short term investments to provide sufficient liquidity for expected disbursements.
3. The maximum percent of callable securities (does not include "make whole call" securities as defined by Glossary) in the portfolio will be 20%.
4. The City may elect to sell a security prior to its maturity and record a capital gain or loss in order to change the portfolio's exposure to market risk.
5. The duration of the portfolio will generally be approximately equal to the duration (typically, plus or minus 20%) of a Market Benchmark, an index selected by the City based on the City's investment objectives, constraints and risk tolerances.

IV. Specific objectives and expectations

- A. Overall objective. The investment portfolio shall be designed with the overall objective of obtaining a total rate of return throughout economic cycles commensurate with investment risk constraints and cash flow needs.
- B. Specific objective. The investment performance objective for the portfolio shall be to earn a total rate of return over a market cycle which is approximately equal to the return on the Benchmark Index. The

Benchmark Index, an index with characteristics similar to those of the portfolio in terms of types of securities and maturities, will be set at the beginning of each year. In addition, an index comprised of U.S. Treasury securities with a maturity distribution similar to that of the Benchmark Index will be presented for comparison purposes.

V. Reporting, disclosure and program evaluation

A. Monthly reports

Monthly investment reports shall be submitted by the Treasurer to the City Manager and the City Council within 30 days of the last day of the month, to be agendized for official action at the second regular Council meeting thereafter. The reports shall also be transmitted to the Investment Advisory Commission on their quarterly meeting agendas, for their review and comment. These reports shall disclose information about the risk characteristics and market value of the City's portfolio in accordance with Governmental Accounting Standards Board Statement No. 31 and shall include:

1. Treasurer's Monthly Report cover page:
  - a) cash receipts, disbursements and balances in total,
  - b) a summary of the portfolio at month-end,
  - c) information regarding interest earnings,
  - d) a statement of compliance with investment policy, including a schedule of any transactions or holdings which do not comply with this policy or with the California Government Code, including a justification for their presence in the portfolio and a timetable for resolution.
  - e) a statement of the City's ability to meet its expenditure requirements for the next six months.
  - f) market value of the portfolio
  - g) sector allocation
2. One-page summary report of portfolio characteristics including modified duration of the portfolio and the benchmark index, average maturity, maturity distribution in years, and time weighted total rate of return.
3. Graphical comparison of the portfolio composition and maturity distribution information for the current month compared to the prior

month.

4. Reconciliation of cash disbursements.
5. Listing of individual investment transactions during the month as required by Government Code section 53607.
6. An asset listing showing type of investment, par value, purchase price, market value, issuer, purchase date, maturity date and yield to maturity.

B. Annual reports

1. The investment policy shall be reviewed and adopted at least annually within the first 90 days of each fiscal year 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.
2. An annual Treasurer's report for the prior fiscal year shall be presented in conjunction with the investment policy review. This report shall include comparisons of the City's return to the Benchmark Index return, shall suggest policies and improvements that might enhance the investment program, and shall include an investment plan for the coming year.
3. The City's comprehensive annual financial report shall include all disclosures regarding cash and investments that are required by Governmental Accounting Standards Board Statement No. 40.

C. Internal controls

The Treasurer is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the entity are protected from loss, theft or misuse. The internal control structure shall be designed to provide reasonable assurance that these objectives are met.

D. Annual audit

The Treasurer shall establish an annual process of independent review by an external auditor to assure compliance with internal controls.

E. Special audits

The City Council may at any time order an audit of the investment portfolio and/or the City Treasurer's investment practices.

F. Independent investment adviser

In its discretion, the City Council may retain the services of an independent investment adviser to review the investment program from time to time. The adviser will review compliance with policies and procedures, independently calculate the market value of the City's holdings, report on overall portfolio risk exposure and investment results, and make recommendations, if needed, regarding investment strategy, risk, or any aspect of the investment program.

G. Investment Advisory Commission

Responsibilities

It shall be the responsibility of the IAC to:

1. Oversee the implementation of the City's investment program, assuring its consistency with the investment policy and recommend changes to the investment policy for consideration by the City Council.
2. Receive and review the monthly investment reports described in Section V (A) at their quarterly meetings.
3. Approve the lists of authorized banks, dealers, brokers and direct issuers used by the City, as well as any additions to or deletions from such lists.
4. Review the City's portfolio activity and performance for suitability and compliance with this policy.
5. Make recommendations to the City Treasurer regarding portfolio activity, performance and compliance with this policy.
6. Make recommendations to the City Council regarding the hiring of external managers and permitted investments and investment strategies for such external managers.
7. Make recommendations to the City Council regarding the use of specific local agency investment pools.
8. Inform the City Council of unaddressed concerns with the management of the City's investment portfolio.

## GLOSSARY OF INVESTMENT TERMS

**Banker's acceptance.** A high quality, short-term money market instrument used to finance international trade. There has never been an instance of a failure to pay a banker's acceptance in full at its maturity date.

**Benchmark.** A segment of the securities market with characteristics similar to the subject portfolio. It is used to compare portfolio performance to the performance of the appropriate segment of the market.

**Collateral.** Securities, evidence of deposits or other property that a borrower pledges to secure repayment of a loan. It also refers to securities pledged by a bank to secure deposits of public monies. In California, repurchase agreements, reverse repurchase agreements, negotiable CDs purchased at a California institution, and public deposits must be collateralized.

**Commercial paper.** Short-term, negotiable unsecured promissory notes of corporations.

**Federal agency securities.** The federal agency securities market is divided into two sectors: the federally related institution securities market and the federally sponsored agency securities market. Federally related institutions are arms of the federal government and their securities are backed by the full faith and credit of the US Government.

Federally sponsored agencies, referred to as government-sponsored entities (GSE's), are privately owned, publicly chartered entities and they issue securities directly in the marketplace. Not all GSE securities are backed by the full faith and credit of the US government including the Federal Farm Credit Bank, Federal Home Loan Bank, Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association.

**Local Agency.** The term local agency shall have the same meaning as set forth in Government Code section 53600.

**Local agency investment fund (LAIF).** A pooled investment vehicle for local agencies in California sponsored by the State of California and administered by the State Treasurer.

**Local agency sponsored investment pool.** A pooled investment vehicle sponsored by a local agency or a group of local agencies for use by other local agencies.

**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."

**Market cycle.** A market cycle is defined as a period of time which includes a minimum of two consecutive quarters of falling interest rates followed by a minimum of two consecutive quarters of rising interest rates.

**Modified duration.** A measure of exposure to market risk of a security or a portfolio. It is the percent change in the price of a security (portfolio) for a 100 basis point change in the security's (portfolio's) yield.

**Negotiable certificate of deposit.** A large denomination certificate of deposit which can be sold in the open market prior to maturity.

**NRSRO. Nationally Recognized Statistical Rating Organization.**

**Repurchase agreement.** An investment transaction wherein an investors agrees to purchase securities at an agreed upon price, and simultaneously agrees to sell the securities back to the contra party on an agreed upon future date at an agreed upon price.

**Time certificate of deposit.** A non-negotiable certificate of deposit which cannot be sold prior to maturity.

**Time-weighted total rate of return.** A measurement of portfolio return which eliminates the effect of the timing of contributions to and withdrawals from the fund.