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Item No. 9

JUN 5 2019

City of South Gate
CITY COUNCIL

CITY OF SOUTH GATE
OFFICE OF THE CITY MANAGER

11:30am

AGENDA BILL

For the Regular Meeting of: June 11, 2019
Originating Department: Administrative Services

Department Director:

Jackie Acosta
Jackie Acosta

City Manager:

Michael Flad
Michael Flad

SUBJECT: ANNUAL ADOPTION OF THE CITY'S INVESTMENT POLICY

PURPOSE: California Government Code Section 53646 requires staff to annually submit the City's Statement of Investment Policy to the City Council.

RECOMMENDED ACTION: Adopt the City's Annual Statement of Investment Policy.

FISCAL IMPACT: None.

ANALYSIS: None.

BACKGROUND: California Government Code Section 53646 requires the City Council to annually adopt an investment policy. This policy was written and adopted in December 2004, and affirmed each year thereafter, with only minor changes.

This year, staff recommends amending section V. B. – Liquidity, such that staff is not limited to only having 30% or less of the portfolio invested for more than one year. This is a restrictive covenant that can preclude the City from appropriately laddering our portfolio and from earning higher interest rates. Total liquidity is measured by cash on hand and "cash equivalents." By purchasing securities that have an active or secondary market, maintaining a healthy LAIF balance, and laddering our investment maturities, we are confident that we can meet our current and expected liquidity needs. Safety is always the City's main concern, and scheduling maturities at different dates, including longer term, adds stability to our projected investment earnings. If 70% of the portfolio is always turning over within one year (because it must be invested for a term of one year or less), a majority of our investment earnings will be substantially affected by short-term interest rate movements. For example, if interest rates go down, 70% of our portfolio will be reinvested at the new lower rate within one year. Rather than positioning our investments based on where we think the market is going, we wish to maintain an objective, rate-agnostic approach where we simply ladder the investments between one and five years. Having the ability to invest more of the portfolio between one and five years will give both the benefit of having an overall portfolio that has laddered (i.e. scheduled) maturities spread out over the next five years and earns more interest, while still appropriately managing liquidity.

The current language in section V. B. is, "The investment portfolio will remain sufficiently liquid to enable the City to meet all operating expenditure requirements which might be reasonably anticipated. In order to maintain liquidity, no more than 30 percent of the portfolio will have a maturity in excess of one (1) year."

Staff is recommending the following changes, "The investment portfolio will remain sufficiently liquid to enable the City to meet all operating expenditure requirements which might be reasonably anticipated. In order to maintain liquidity, **the City will develop a laddered investment portfolio with regularly scheduled maturities and invest primarily in securities with active secondary or resale markets.**"

Even with the proposed change, the City's investment policy continues to be very conservative, authorizing only those investments provided for in the Government Code. It requires diversification of the City's investments, with no maturity exceeding five years, and all brokers must be pre-screened before investing any of the City's funds.

ATTACHMENTS: A. Proposed Statement of Investment Policy
B. Current Statement of Investment Policy with red-lined changes

STATEMENT OF INVESTMENT POLICY

I. POLICY

It is the policy of the City of South Gate, referred to as "City," to invest public funds in a prudent manner which will provide, in the following order: 1) the highest level of safety of funds, 2) liquidity of funds in order that daily cash flow demands are met, and 3) that the yield or investment return be maximized, all while conforming to all laws of the State of California regarding the investment of public funds.

In accordance with Section 53646 of the Government Code, the Director of Administrative Services, hereafter referred to as "Director", will annually render to the City Council a Statement of Investment Policy. The Director, City Treasurer, City Manager and the City Council Finance Committee shall review the policy on an annual basis for submission and approval by the City Council.

II. DELEGATION OF AUTHORITY

The City Council, consistent with Government Code Section 53601, has retained investment authority and is ultimately responsible for all investment decisions. The authority for administration of the City's investment program is vested with the Director as a general extension of the powers and duties of the Director pursuant to Chapter 1.08 of the South Gate Municipal code, and further, pursuant to the City Council action of February 25, 1997. As administrator of the City's financial program, the Director is assigned full discretionary management of the City's investments and shall report directly to the City Council. The appointment of the Director as administrator of the City's investment program shall be annually reviewed by the City Council pursuant to the City's statement of investment policy. In the absence of the Director of Administrative Services, the City Council delegates the City Manager as administrator.

III. SCOPE

The Director is authorized to invest the City's funds in accordance with California Government Code Sections 16429.1 and 53601 et seq. This investment policy applies to all financial assets of the City. These funds are accounted for in the Comprehensive Annual Financial Report (CAFR), which includes the following fund types:

- General Fund
- Special Revenue
- Debt Service
- Capital Projects
- Enterprise
- Internal Services
- Trust and Agency
- Any new fund created by the legislative body, unless specifically exempted.

All monies entrusted to the Director will be pooled in the portfolio except for the employee's retirement funds which are administered separately, and the proceeds of certain debt issues which are managed and invested by trustees appointed under indenture agreements.

IV. PRUDENCE

According to Section 53600.3 of the California Government Code, the governing body, or persons authorized to make investment decisions on behalf of the local agency, are trustees and therefore fiduciaries subject to the prudent investor standard. The actions of the Director in the performance of his/her duties as manager of public funds shall be evaluated using the following prudent person standard applied in the context of managing the overall portfolio:

Investments shall be made with judgment and care under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation but for investment, considering the probable safety of their capital as well as the probable income to be derived.

Investment officers acting in accordance with written procedures and the investment policy 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.

V. OBJECTIVES

In accordance with Section 53600.5 of the Government Code, the primary objectives of the City's investment activities shall be in priority order:

A. Safety

Safety 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 City shall seek to safeguard principal by a careful examination of credit risk and market risk of individual investments.

1. *Credit Risk* – is defined as the risk of loss due to failure of an issuer of a security and shall be mitigated by investing in only very safe institutions and by diversifying the fund so that the failure of any one issuer would not unduly harm the City's cash flow.
2. *Market Risk* – is defined as the risk of market value fluctuations due to overall changes in the general level of interest rates and shall be mitigated by limiting the weighted average maturity of the City fund to less than five years.

B. Liquidity

The investment portfolio will remain sufficiently liquid to enable the City to meet all operating expenditure requirements which might be reasonably anticipated. In order to maintain liquidity, the City will develop a laddered investment portfolio with regularly scheduled maturities and invest primarily in securities with active secondary or resale markets.

C. Return on Investment

The City's investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and the cash flow characteristics of the portfolio. Whenever possible, consistent with risk limitations and prudent investment principles, the City shall make an effort to achieve returns at the market-average rate of returns. The market-average rate of return is defined as the average return on three-month U.S. Treasury Bills or the Local Agency Investment Fund administered by the California State Treasurer. These indices are considered benchmarks for lower risk investment transactions and therefore comprise a minimum standard for the portfolio's rate of return. The investment program shall seek to augment returns above this threshold, consistent with risk limitations identified herein and prudent investment policies.

Because the City operates the portfolio passively, the Director applies a buy and hold philosophy to the acquisition and sale of individual investments.

VI. SAFEKEEPING AND CUSTODY

A. Delivery vs. Payment

All trades of marketable securities will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible financial institution prior to release of the City funds.

B. Safekeeping

Securities will be held by an independent third-party custodian selected by the City as evidenced by safekeeping receipts in the City's name and annually provide a financial report.

C. Internal Controls

The Director is responsible for ensuring compliance with the City's investment policies as well as for establishing systems of internal control to ensure the assets of the City are protected from loss, theft or misuse and to regulate the activities of subordinate staff.

The internal controls structure shall address the following points:

- Control of collusion
- Separation of transaction authority from accounting and recordkeeping

- Custodial safekeeping
- Avoidance of physical delivery of securities
- Clear delegation of authority to subordinate staff
- Written confirmation of transactions for investments and wire transfers
- Dual authorizations of wire transfers
- Development of a wire transfer agreement with the lead bank and third-party custodian

Accordingly, the City Council will be assured the portfolio complies with policies and procedures during the annual independent audit by the City's external auditor.

VII. ETHICS AND CONFLICTS OF INTEREST

Officers and employees involved in the investment process 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. The Director is required to file annual disclosure statements as required by the Fair Political Practices Commission (EPPC), thus disclosing to the City Clerk any material financial interests in financial institutions that conduct business within this jurisdiction. Officers and employees involved in the investment process shall further disclose any large personal financial investment positions that could be related to the performance of the City investment portfolio.

During the course of the year, if there is an event subject to disclosure that could impair the ability of the Director to make impartial decisions the City Manager will be notified in writing within 10 days.

VIII. AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS

Pursuant to the State Code, Section 53601.5, the City shall transact business only with issuers, banks, savings and loans and registered investment securities dealers. The purchase of any investment, other than those purchased directly from the issuer, shall be purchased either from an institution licensed by the State of California as a broker/dealer, as defined in section 25004 of the Corporations code, who is a member of the National Association of Securities Dealers or a member of a Federally regulated securities exchange, a National or State-Chartered Bank, a Federal or State Association (as defined by Section 5102 of the Financial Code), or a brokerage firm designated as a Primary Government Dealer by the Federal Reserve Bank. The Director's staff shall investigate all institutions that wish to do business with the City in order to determine if they are adequately capitalized, make markets in securities appropriate to the City's needs by completing and signing a Broker-Dealer Questionnaire (Appendix A), agree by signing the Broker-Dealer Receipt of Investment Policy (Appendix B) to abide by the conditions set forth in the City's Investment Policy and provide a current audited financial statement annually.

The Director will maintain a list of financial institutions authorized to provide investment services to the City, will not give full discretionary authority to external investment managers

and will not use external investment managers to purchase or sell securities or manage the City's portfolio unless specifically approved by the City Council with a contract signed by the Mayor and City Attorney.

IX. AUTHORIZED AND SUITABLE INVESTMENTS

The State of California Government Code Sections 16429.1 and 53601 et seq., limit the investment vehicles available to local agencies. The City's Investment Policy further restricts the permitted investments to those listed below:

- State Treasurer's Local Agency Investment Fund (LAIF) – Government Code Section 16429.1 authorizes each local government agency to invest a maximum of \$65 million in this investment program administered by the California State Treasurer. Money invested with LAIF is pooled with State money in order to earn the maximum rate of return possible in a manner consistent with sound investment practices.
- United States Treasury Bills, Notes and Bonds or those for which the full faith and credit of the United States are pledged for payment of principal and interest. Purchase of this category shall not exceed five years to maturity. There is no percentage limit in this category.
- Federal Agency or United States government sponsored securities including those issued by or fully guaranteed as to principle and interest by federal agencies or United States government-sponsored enterprises. Obligations in this in this category referred to as "Federal Agencies" include but are not limited to issues by the Government National Mortgage Association, Federal Mortgage Association and Federal Home Loan Mortgage Corporation. There are no restrictions in amount of purchase or percentage of holdings.
- Time Certificates of Deposits – As authorized in Government Code Section 53601 and 53630, Time Certificates of Deposits are fixed term investments which are required to be collateralized from 110% to 150% depending on the specific security pledged as security. The City shall deposit funds only with financial institutions which operate in California. The Federal Deposit Insurance Corporation (FDIC) must insure these institutions. There are no portfolio limits on limits on the amount or maturity for this type of investment.
- Negotiable Certificates of Deposits – As authorized in Government Code Section 53601(i), Negotiable Certificates of Deposit are short-term investments issued by a nationally or state-chartered bank. Purchases may not exceed 30% of the portfolio and final maturity may not exceed five (5) years from date of purchase.
- Certificate of Deposit Account Registry System (CDARS) - A private CD placement service that allows local agencies to purchase more than \$250,000 in CDs from a single financial institution (must be a participating institution of CDARS) while still maintaining FDIC insurance coverage. CDARS facilitates the trading of deposits between the California institution and other participating institutions in amounts that are less than \$250,000 each,

so that FDIC coverage is maintained.

- **Bankers Acceptances** – otherwise known as bills of exchange or time drafts that are drawn on and accepted by a commercial bank. Purchase of banker's acceptances may not exceed 180 days (six months) maturity or 40% of the agency's portfolio that may be invested. Moreover, no more than 30% of the City's portfolio may be invested in the banker's acceptances of any commercial bank.
- **Commercial Paper** – of "prime" quality of the highest ranking or of the highest letter and number rating provided by Moody's Investors Service, Inc., Standard and Poor's (S&P) or Fitch Financial Services, Inc. (Fitch). The corporation that issues the commercial paper shall be organized and operating within the United States, shall have total assets debt, other than commercial paper that is rated "A" or higher by Moody's, S&P or Fitch. Eligible commercial paper shall have a maximum maturity of 270 days or less and not represent more than 10% of the outstanding paper of an issuing corporation. The City may not invest more than 25% of the portfolio in eligible commercial paper.
- **Medium – Term Notes** – defined as all corporate and depository institutions debt securities with a maximum remaining maturity of five years or less, issued by corporations organized within the United States or by institutions licensed by the United States or any state and operating within the United States. Notes must be rated category "A" or its equivalent or better by a nationally recognized rating service. No more than 10% of the portfolio may be invested in one bank or corporate name. If rated by more than one rating service, both ratings must meet the minimum credit standards. Purchases of medium-term notes shall not exceed 30% of the agency's portfolio.
- **Bond Funds and Money Market Mutual Funds** – Shares of beneficial interest issued by diversified management companies investing in the securities and obligations as authorized by the State of California Code 53601 and 52630 et seq. Both investments must have assets under management in excess of five hundred million dollars (\$500,000,000) and the purchase price may not include any commissions charged by these companies. These types of investments are to be used primarily as overnight or short term sweep accounts for interest and maturities with the City's custodial agent and the City's bank accounts. Companies must have either:
 - 1) The highest ranking or the highest letter and numerical rating provided by not less than two of the nationally recognized rating, or
 - 2) Retained an investment advisor registered or exempt with the Securities and Exchange Commission, with no less than five years of experience investing in:
 - a) Bond Funds – the securities and obligations authorized by the State Code 53601 a-j inclusive and 1 or m; or
 - b) Money Market Mutual Funds – money mutual funds.

Investments shall be purchased and sold through a competitive bid/offer process. Bids/offers for securities of comparable maturity, credit and liquidity shall be received

from at least three financial institutions, when possible.

Where this section specifies a percentage limitation for a particular category of investment, that percentage is applicable only at the date of purchase. Where this section specifies time-specific, that is only applicable at the date of purchase.

- According to State of California Code 53601.6, the City may not invest in inverse floaters, range notes or mortgage derived, interest-only strips.

X. COLLATERALIZATION

Pursuant to State Code, Sections 53651-53667, depositories have duties and responsibilities toward public monies on deposit that may differ from their duties relative to nonpublic funds. California law requires public funds to be collateralized – the depository must secure its public fund accounts by maintaining with the agent of the depository securities having a market value of at least one hundred ten percent (110%) of the value of the public funds accounts (see Government Code Section 53652). If a depository uses mortgage-backed securities as collateral for public funds, the market value of the securities must be at least 150% of the value of the public funds. A waiver may be granted under certain circumstances or to the extent the City funds are insured by the Federal Deposit Insurance Corporation (FDIC).

XI. DIVERSIFICATION

The City will diversify its investments by security type and institution. With the exception of U.S. Treasury securities, federal agency securities, overnight sweep accounts, and authorized pools (LAIF), no more than 20% of the entity's total investment portfolio will be invested in a single security type or 10% in any one corporate or bank issuer.

XII. MAXIMUM MATURITIES

To the extent possible, the City will attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the City will not directly invest in securities maturing more than five (5) years from the date of purchase.

XIII. POLICY CONSIDERATIONS

Any investment currently held that does not meet the guidelines of this policy shall be exempted from the requirements of this policy. The City Council will be advised of the situation and intended course of action. At maturity or liquidation, such monies shall be reinvested only as provided by this policy.

XIV. REPORTING

Under the provision of Section 53646 of the California Government Code, the Director shall render a report to the City Council and the City Manager containing detailed information on

all securities, investments and moneys of the City. The report will be submitted on at least a quarterly basis and provided to the City Council within 30 days following the end of the quarter.

The report will contain the following information that is subject to this investment policy:

- 1) the type of investment, name of the issuer, date of maturity, par and cost in each investment;
- 2) the weighted average maturity of the investments;
- 3) any investments, including loans and security lending programs, that are under the management of contracted parties;
- 4) the market value and source of the valuation to ensure that review of investments in terms of value and price volatility have been performed;
- 5) a description of the compliance with the statement of investment policy;
- 6) level of custodial risk; and
- 7) a statement denoting the City's ability to meet its anticipated expenditure requirements for the next six months.

ATTACHMENTS: A) GLOSSARY
 B) APPENDIX A - BROKER-DEALER QUESTIONNAIRE
 C) APPENDIX B - BROKER-DEALER RECEIPT OF INVESTMENT POLICY

GLOSSARY

AGENCY: Federal agency securities.

ASKED: The price at which securities are offered.

BANKERS' ACCEPTANCE (BA): A draft or bill exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the insurer.

BID: The price offered for securities.

BROKER: A broker brings buyers and sellers together for a commission.

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.

CERTIFICATE OF DEPOSIT (CD): A time deposit with a specific maturity evidenced by a certificate. Certificate of Deposit may be issued in either negotiable or nonnegotiable form. Nonnegotiable certificates cannot be resold in the secondary market and may face penalties for early redemption whereas a negotiable CD may be resold.

CERTIFICATE OF DEPOSIT ACCOUNT REGISTRY SYSTEM (CDARS): A private CD placement service that allows local agencies to purchase more than \$250,000 in CDs from a single financial institution (must be a participating institution of CDARS) while still maintaining FDIC insurance coverage. CDARS is currently the only entity providing this service. CDARS facilitates the trading of deposits between the California institution and other participating institutions in amounts that are less than \$250,000 each, so that FDIC coverage is maintained.

COUPON: (a) The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value. (b) A certificate attached to a bond evidencing interest due on a payment date.

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

DEBENTURE: A bond secured only by the general credit of the issuer.

DISCOUNT: The difference between the cost price of a security and its value at maturity when quoted at lower than face value. A security selling below original offering price shortly after sale also is considered to be at a discount.

DISCOUNT SECURITIES: Non-interest bearing money market instruments that are issued at a discount and redeemed at maturity for full value, e.g. US Treasury Bills.

DIVERSIFICATION: Dividing investment funds among a variety of securities offering independent return.

FEDERAL CREDIT AGENCIES: Agencies of 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 cooperatives and exporters.

FEDERAL FUNDS RATE: The rate of interest at which Fed funds are traded. The Federal Reserve through open-market operations currently pegs this rate.

FEDERAL RESERVE SYSTEM: The Central Bank of the United States created by Congress and consisting of a seven Board of Governors in Washington, D.C., 12 Regional Banks and about 5,700 commercial banks that are members of the system.

FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC): A federal agency that insures bank deposits, currently up to \$100,000 per deposit.

FEDERAL HOME LOAN BANKS (FHLB): The institutions that regulate lend to savings and loan associations and other institutions. Security holder is protected by the full faith and credit of the U.S. Government. Ginnie Mae securities are backed by FHA, VA or FMHM mortgages.

LIQUIDITY: A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value.

LOCAL AGENCY INVESTMENT FUND (LAIF): The aggregate of all funds from political subdivisions that are placed in the custody of the State Treasurer for investment and reinvestment.

MARKET VALUE: The price at which a security is trading and could presumably be purchased or sold.

MATURITY: The date upon which the principal or stated value of an investment becomes due and payable.

MONEY MARKET: The market in which short-term debt instruments (US T-bills, commercial paper, bankers' acceptances, etc.) are issued and traded.

NEGOTIABLE CERTIFICATES OF DEPOSIT: Short-term debt instrument that usually pays interest and is issued by a bank, savings or federal association, state or federal credit union, or state-licensed branch of a foreign bank. The majority of negotiable CDs mature within six months while the average maturity is two weeks. Negotiable CDs are traded in a secondary market and are payable upon order to the bearer or initial depositor (investor). Negotiable CDs are insured by FDIC up to \$250,000, but they are not collateralized beyond that amount.

PORTFOLIO: The collection of securities held by an investor.

PRUDENT PERSON RULE: An investment standard. In some states the law requires that a fiduciary, such as a trustee, may invest money only in a list of securities selected by the state-the so-called legal list. In other states the trustee may invest in a surety if it is one, which a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital would buy.

PRIMARY DEALER: A group of government securities dealers that submit daily reports of market and positions 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.

RATE OF RETURN: For fixed-rate securities, it is the coupon or contractual dividend rate divided by the purchase price, which is also the current yield.

QUALIFIED PUBLIC DEPOSITORIES: A financial institution which does not claim exemption from the payment of any sales or compensating use or ad valorem taxes under the laws of this state, which has segregated for the benefit of the commission eligible collateral having a value of not less than its maximum liability and which has been approved by the Public Deposit Protection Commission to hold public deposits.

SAFEKEEPING: 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 vaults for protection.

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

SECURITIES & EXCHANGE COMMISSION: Agency created by Congress to protect investors in securities transactions by administering securities legislation.

TREASURY BILLS OR T-BILLS: A non-interest bearing discount security issued by the US Treasury to finance the national debt. Most bills are issued to mature in three months, six months or one year.

TREASURY BOND: Long-term US Treasury securities having initial maturities of more than ten years.

TREASURY NOTES: Intermediate term coupon bearing US Treasury securities issued as direct obligations of the US Government and having initial maturities of from one to ten years.

YIELD: The rate of annual income return on an investment, expressed as a percentage.

10. Please provide your Wiring and Delivery instructions.

11. Which of the following instruments are offered regularly by your local desk:

- T-Bills Treasury Notes/Bonds Discount Notes NCD's
- Agencies (specify) _____
- BA's (Domestic) BA's (Foreign) Commercial Paper
- Medium-Term Notes

12. Does your Firm specialize in any of the instruments listed above? _____

13. Please identify your comparable government agency clients in the City of South Gate's geographical area.

14. What reports, confirmation, and other documentation would the City receive?

15. Please include samples of research reports or market information that your firm regularly provides to government agency clients.

16. What precautions are taken by your Firm to protect the interests of the public when dealing with government agencies as investors?

17. Have you or your Firm been censured, sanctioned or disciplined by a Regulatory State or Federal Agency for improper or fraudulent activities, related to the sale of securities within the past five years? [] Yes [] No

18. If yes, please explain. _____

19. Attached certified document of your capital adequacy and financial solvency. In addition, an audited financial statement must be provided currently, and within 120 days of your fiscal year-end.

20. Please indicate the current licenses of the City's representatives:

Agent _____ License or registration _____

21. Is your firm a member of the NASD? Does it subscribe to the rules of fair practice?

APENDIX B

BROKER-DEALER RECEIPT OF INVESTMENT POLICY

We are in receipt of the City of South Gate's Investment Policy.

We have read the policy and understand the provisions and guidelines of the policy. All salespersons covering the City's account will be made aware of this policy and will be directed to give consideration to its provisions and constraints in selecting investment opportunities to present to the City.

SIGNATURES:

_____ Firm

_____ Firm

_____ Name

_____ Name

_____ Title

_____ Title

Date: _____

Date: _____

After reading and signing this Receipt of Investment Policy, please return with supporting documentation to:

City of South Gate
Director of Administrative Services
8650 California Avenue
South Gate, CA 90280-3075

City of South Gate's Use Only:

Approved: _____

Disapproved: _____

Date: _____

Signature: _____

Date notification sent: _____

Sent by: _____

STATEMENT OF INVESTMENT POLICY

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A. Delivery vs. Payment

All trades of marketable securities will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible financial institution prior to release of the City funds.

B. Safekeeping

Securities will be held by an independent third-party custodian selected by the City as evidenced by safekeeping receipts in the City's name and annually provide a financial report.

C. Internal Controls

The Director is responsible for ensuring compliance with the City's investment policies as well as for establishing systems of internal control to ensure the assets of the City are protected from loss, theft or misuse and to regulate the activities of subordinate staff.

The internal controls structure shall address the following points:

- Control of collusion

- Separation of transaction authority from accounting and recordkeeping
- Custodial safekeeping
- Avoidance of physical delivery of securities
- Clear delegation of authority to subordinate staff
- Written confirmation of transactions for investments and wire transfers
- Dual authorizations of wire transfers
- Development of a wire transfer agreement with the lead bank and third-party custodian

Accordingly, the City Council will be assured the portfolio complies with policies and procedures during the annual independent audit by the City's external auditor.

VII. ETHICS AND CONFLICTS OF INTEREST

Officers and employees involved in the investment process 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. The Director is required to file annual disclosure statements as required by the Fair Political Practices Commission (EPPC), thus disclosing to the City Clerk any material financial interests in financial institutions that conduct business within this jurisdiction. Officers and employees involved in the investment process shall further disclose any large personal financial investment positions that could be related to the performance of the City investment portfolio.

During the course of the year, if there is an event subject to disclosure that could impair the ability of the Director to make impartial decisions the City Manager will be notified in writing within 10 days.

VIII. AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS

Pursuant to the State Code, Section 53601.5, the City shall transact business only with issuers, banks, savings and loans and registered investment securities dealers. The purchase of any investment, other than those purchased directly from the issuer, shall be purchased either from an institution licensed by the State of California as a broker/dealer, as defined in section 25004 of the Corporations code, who is a member of the National Association of Securities Dealers or a member of a Federally regulated securities exchange, a National or State-Chartered Bank, a Federal or State Association (as defined by Section 5102 of the Financial Code), or a brokerage firm designated as a Primary Government Dealer by the Federal Reserve Bank. The Director's staff shall investigate all institutions that wish to do business with the City in order to determine if they are adequately capitalized, make markets in securities appropriate to the City's needs by completing and signing a Broker-Dealer Questionnaire (Appendix A), agree by signing the Broker-Dealer Receipt of Investment Policy (Appendix B) to abide by the conditions set forth in the City's Investment Policy and provide a current audited financial statement annually.

The Director will maintain a list of financial institutions authorized to provide investment

services to the City, will not give full discretionary authority to external investment managers and will not use external investment managers to purchase or sell securities or manage the City's portfolio unless specifically approved by the City Council with a contract signed by the Mayor and City Attorney.

IX. AUTHORIZED AND SUITABLE INVESTMENTS

The State of California Government Code Sections 16429.1 and 53601 et seq., limit the investment vehicles available to local agencies. The City's Investment Policy further restricts the permitted investments to those listed below:

- State Treasurer's Local Agency Investment Fund (LAIF) – Government Code Section 16429.1 authorizes each local government agency to invest a maximum of \$65 million in this investment program administered by the California State Treasurer. Money invested with LAIF is pooled with State money in order to earn the maximum rate of return possible in a manner consistent with sound investment practices.
- United States Treasury Bills, Notes and Bonds or those for which the full faith and credit of the United States are pledged for payment of principal and interest. Purchase of this category shall not exceed five years to maturity. There is no percentage limit in this category.
- Federal Agency or United States government sponsored securities including those issued by or fully guaranteed as to principle and interest by federal agencies or United States government-sponsored enterprises. Obligations in this in this category referred to as "Federal Agencies" include but are not limited to issues by the Government National Mortgage Association, Federal Mortgage Association and Federal Home Loan Mortgage Corporation. There are no restrictions in amount of purchase or percentage of holdings.
- Time Certificates of Deposits – As authorized in Government Code Section 53601 and 53630, Time Certificates of Deposits are fixed term investments which are required to be collateralized from 110% to 150% depending on the specific security pledged as security. The City shall deposit funds only with financial institutions which operate in California. The Federal Deposit Insurance Corporation (FDIC) must insure these institutions. There are no portfolio limits on limits on the amount or maturity for this type of investment.
- Negotiable Certificates of Deposits – As authorized in Government Code Section 53601(i), Negotiable Certificates of Deposit are short-term investments issued by a nationally or state-chartered bank. Purchases may not exceed 30% of the portfolio and final maturity may not exceed five (5) years from date of purchase.
- Certificate of Deposit Account Registry System (CDARS) - A private CD placement service that allows local agencies to purchase more than \$250,000 in CDs from a single financial institution (must be a participating institution of CDARS) while still maintaining FDIC insurance coverage. CDARS facilitates the trading of deposits between the California

institution and other participating institutions in amounts that are less than \$250,000 each, so that FDIC coverage is maintained.

- **Bankers Acceptances** – otherwise known as bills of exchange or tie drafts that are drawn on and accepted by a commercial bank. Purchase of banker’s acceptances may not exceed 180 days (six months) maturity or 40% of the agency’s portfolio that may be invested. Moreover, no more than 30% of the City’s portfolio may be invested in the banker’s acceptances of any commercial bank.
- **Commercial Paper** – of “prime” quality of the highest ranking or of the highest letter and number rating provided by Moody’s Investors Service, Inc., Standard and Poor’s (S&P) or Fitch Financial Services, Inc. (Fitch). The corporation that issues the commercial paper shall be organized and operating within the United States, shall have total assets debt, other than commercial paper that is rated “A” or higher by Moody’s, S&P or Fitch. Eligible commercial paper shall have a maximum maturity of 270 days or less and not represent more than 10% of the outstanding paper of an issuing corporation. The City may not invest more than 25% of the portfolio in eligible commercial paper.
- **Medium – Term Notes** – defined as all corporate and depository institutions debt securities with a maximum remaining maturity of five years or less, issued by corporations organized within the United States or by institutions licensed by the United States or any state and operating within the United States. Notes must be rated category “A” or its equivalent or better by a nationally recognized rating service. No more than 10% of the portfolio may be invested in one bank or corporate name. If rated by more than one rating service, both ratings must meet the minimum credit standards. Purchases of medium-term notes shall not exceed 30% of the agency’s portfolio.
- **Bond Funds and Money Market Mutual Funds** – Shares of beneficial interest issued by diversified management companies investing in the securities and obligations as authorized by the State of State of California Code 53601 and 52630 et seq. Both investments must have assets under management in excess of five hundred million dollars (\$500,000,000) and the purchase price may not include any commissions charged by these companies. These types of investments are to be used primarily as overnight or short term sweep accounts for interest and maturities with the City’s custodial agent and the City’s bank accounts. Companies must have either:
 - 1) The highest ranking or the highest letter and numerical rating provided by not less than two of the nationally recognized rating, or
 - 2) Retained an investment advisor registered or exempt with the Securities and Exchange Commission, with no less than five years of experience investing in:
 - a) Bond Funds – the securities and obligations authorized by the State Code 53601 a-j inclusive and 1 or m; or
 - b) Money Market Mutual Funds – money mutual funds.

Investments shall be purchased and sold through a competitive bid/offer process.

Bids/offers for securities of comparable maturity, credit and liquidity shall be received from at least three financial institutions, when possible.

Where this section specifies a percentage limitation for a particular category of investment, that percentage is applicable only at the date of purchase. Where this section specifies time-specific, that is only applicable at the date of purchase.

- According to State of California Code 53601.6, the City may not invest in inverse floaters, range notes or mortgage derived, interest-only strips.

X. COLLATERALIZATION

Pursuant to State Code, Sections 53651-53667, depositories have duties and responsibilities toward public monies on deposit that may differ from their duties relative to nonpublic funds. California law requires public funds to be collateralized – the depository must secure its public fund accounts by maintaining with the agent of the depository securities having a market value of at least one hundred ten percent (110%) of the value of the public funds accounts (see Government Code Section 53652). If a depository uses mortgage-backed securities as collateral for public funds, the market value of the securities must be at least 150% of the value of the public funds. A waiver may be granted under certain circumstances or to the extent the City funds are insured by the Federal Deposit Insurance Corporation (FDIC).

XI. DIVERSIFICATION

The City will diversify its investments by security type and institution. With the exception of U.S. Treasury securities, federal agency securities, overnight sweep accounts, and authorized pools (LAIF), no more than 20% of the entity's total investment portfolio will be invested in a single security type or 10% in any one corporate or bank issuer.

XII. MAXIMUM MATURITIES

To the extent possible, the City will attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the City will not directly invest in securities maturing more than five (5) years from the date of purchase.

XIII. POLICY CONSIDERATIONS

Any investment currently held that does not meet the guidelines of this policy shall be exempted from the requirements of this policy. The City Council will be advised of the situation and intended course of action. At maturity or liquidation, such monies shall be reinvested only as provided by this policy.

XIV. REPORTING

Under the provision of Section 53646 of the California Government Code, the Director shall

render a report to the City Council and the City Manager containing detailed information on all securities, investments and moneys of the City. The report will be submitted on at least a quarterly basis and provided to the City Council within 30 days following the end of the quarter.

The report will contain the following information that is subject to this investment policy:

- 1) the type of investment, name of the issuer, date of maturity, par and cost in each investment;
- 2) the weighted average maturity of the investments;
- 3) any investments, including loans and security lending programs, that are under the management of contracted parties;
- 4) the market value and source of the valuation to ensure that review of investments in terms of value and price volatility have been performed;
- 5) a description of the compliance with the statement of investment policy;
- 6) level of custodial risk; and
- 7) a statement denoting the City's ability to meet its anticipated expenditure requirements for the next six months.

ATTACHMENTS: A) GLOSSARY
 B) APPENDIX A - BROKER-DEALER QUESTIONNAIRE
 C) APPENDIX B - BROKER-DEALER RECEIPT OF INVESTMENT POLICY

GLOSSARY

AGENCY: Federal agency securities.

ASKED: The price at which securities are offered.

BANKERS' ACCEPTANCE (BA): A draft or bill exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the insurer.

BID: The price offered for securities.

BROKER: A broker brings buyers and sellers together for a commission.

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.

CERTIFICATE OF DEPOSIT (CD): A time deposit with a specific maturity evidenced by a certificate. Certificate of Deposit may be issued in either negotiable or nonnegotiable form. Nonnegotiable certificates cannot be resold in the secondary market and may face penalties for early redemption whereas a negotiable CD may be resold.

CERTIFICATE OF DEPOSIT ACCOUNT REGISTRY SYSTEM (CDARS): A private CD placement service that allows local agencies to purchase more than \$250,000 in CDs from a single financial institution (must be a participating institution of CDARS) while still maintaining FDIC insurance coverage. CDARS is currently the only entity providing this service. CDARS facilitates the trading of deposits between the California institution and other participating institutions in amounts that are less than \$250,000 each, so that FDIC coverage is maintained.

COUPON: (a) The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value. (b) A certificate attached to a bond evidencing interest due on a payment date.

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

DEBENTURE: A bond secured only by the general credit of the issuer.

DISCOUNT: The difference between the cost price of a security and its value at maturity when quoted at lower than face value. A security selling below original offering price shortly after sale also is considered to be at a discount.

DISCOUNT SECURITIES: Non-interest bearing money market instruments that are issued at a discount and redeemed at maturity for full value, e.g. US Treasury Bills.

DIVERSIFICATION: Dividing investment funds among a variety of securities offering independent return.

FEDERAL CREDIT AGENCIES: Agencies of 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 cooperatives and exporters.

FEDERAL FUNDS RATE: The rate of interest at which Fed funds are traded. The Federal Reserve through open-market operations currently pegs this rate.

FEDERAL RESERVE SYSTEM: The Central Bank of the United States created by Congress and consisting of a seven Board of Governors in Washington, D.C., 12 Regional Banks and about 5,700 commercial banks that are members of the system.

FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC): A federal agency that insures bank deposits, currently up to \$100,000 per deposit.

FEDERAL HOME LOAN BANKS (FHLB): The institutions that regulate lend to savings and loan associations and other institutions. Security holder is protected by the full faith and credit of the U.S. Government. Ginnie Mae securities are backed by FHA, VA or FMHM mortgages.

LIQUIDITY: A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value.

LOCAL AGENCY INVESTMENT FUND (LAIF): The aggregate of all funds from political subdivisions that are placed in the custody of the State Treasurer for investment and reinvestment.

MARKET VALUE: The price at which a security is trading and could presumably be purchased or sold.

MATURITY: The date upon which the principal or stated value of an investment becomes due and payable.

MONEY MARKET: The market in which short-term debt instruments (US T-bills, commercial paper, bankers' acceptances, etc.) are issued and traded.

NEGOTIABLE CERTIFICATES OF DEPOSIT: Short-term debt instrument that usually pays interest and is issued by a bank, savings or federal association, state or federal credit union, or state-licensed branch of a foreign bank. The majority of negotiable CDs mature within six months while the average maturity is two weeks. Negotiable CDs are traded in a secondary market and are payable upon order to the bearer or initial depositor (investor). Negotiable CDs are insured by FDIC up to \$250,000, but they are not collateralized beyond that amount.

PORTFOLIO: The collection of securities held by an investor.

PRUDENT PERSON RULE: An investment standard. In some states the law requires that a fiduciary, such as a trustee, may invest money only in a list of securities selected by the state-the so-called legal list. In other states the trustee may invest in a surety if it is one, which a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital would buy.

PRIMARY DEALER: A group of government securities dealers that submit daily reports of market and positions 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.

RATE OF RETURN: For fixed-rate securities, it is the coupon or contractual dividend rate divided by the purchase price, which is also the current yield.

QUALIFIED PUBLIC DEPOSITORIES: A financial institution which does not claim exemption from the payment of any sales or compensating use or ad valorem taxes under the laws of this state, which has segregated for the benefit of the commission eligible collateral having a value of not less than its maximum liability and which has been approved by the Public Deposit Protection Commission to hold public deposits.

SAFEKEEPING: 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 vaults for protection.

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

SECURITIES & EXCHANGE COMMISSION: Agency created by Congress to protect investors in securities transactions by administering securities legislation.

TREASURY BILLS OR T-BILLS: A non-interest bearing discount security issued by the US Treasury to finance the national debt. Most bills are issued to mature in three months, six months or one year.

TREASURY BOND: Long-term US Treasury securities having initial maturities of more than ten years.

TREASURY NOTES: Intermediate term coupon bearing US Treasury securities issued as direct obligations of the US Government and having initial maturities of from one to ten years.

YIELD: The rate of annual income return on an investment, expressed as a percentage.

10. Please provide your Wiring and Delivery instructions.

11. Which of the following instruments are offered regularly by your local desk:

- T-Bills Treasury Notes/Bonds Discount Notes NCD's
- Agencies (specify) _____
- BA's (Domestic) BA's (Foreign) Commercial Paper
- Medium-Term Notes

12. Does your Firm specialize in any of the instruments listed above? _____

13. Please identify your comparable government agency clients in the City of South Gate's geographical area.

14. What reports, confirmation, and other documentation would the City receive?

15. Please include samples of research reports or market information that your firm regularly provides to government agency clients.

16. What precautions are taken by your Firm to protect the interests of the public when dealing with government agencies as investors?

17. Have you or your Firm been censored, sanctioned or disciplined by a Regulatory State or Federal Agency for improper or fraudulent activities, related to the sale of securities within the past five years? [] Yes [] No

18. If yes, please explain. _____

19. Attached certified document of your capital adequacy and financial solvency. In addition, an audited financial statement must be provided currently, and within 120 days of your fiscal year-end.

20. Please indicate the current licenses of the City's representatives:

Agent _____ License or registration _____

21. Is your firm a member of the NASD? Does it subscribe to the rules of fair practice?

APENDIX B

BROKER-DEALER RECEIPT OF INVESTMENT POLICY

We are in receipt of the City of South Gate's Investment Policy.

We have read the policy and understand the provisions and guidelines of the policy. All salespersons covering the City's account will be made aware of this policy and will be directed to give consideration to its provisions and constraints in selecting investment opportunities to present to the City.

SIGNATURES:

_____ Firm

_____ Firm

_____ Name

_____ Name

_____ Title

_____ Title

Date: _____

Date: _____

After reading and signing this Receipt of Investment Policy, please return with supporting documentation to:

City of South Gate
Director of Administrative Services
8650 California Avenue
South Gate, CA 90280-3075

City of South Gate's Use Only:

Approved: _____

Disapproved: _____

Date: _____

Signature: _____

Date notification sent: _____

Sent by: _____