Concord

REPORT TO MAYOR/REDEVELOPMENT AGENCY CHAIR AND COUNCIL/AGENCY BOARD

TO THE HONORABLE MAYOR/REDEVELOPMENT AGENCY CHAIR AND CITY COUNCIL/AGENCY BOARD:

DATE: June 22, 2009

SUBJECT: CITY OF CONCORD AND CONCORD REDEVELOPMENT AGENCY INVESTMENT POLICY

Report in Brief

The purpose of this recommended action is to comply with Government Code Section 53646, which requires the annual approval of a formal investment policy by the legislative body at a public meeting.

Background

Several years ago, in response to the Orange County investment debacle, the State Legislature enacted several bills which it felt would help prevent other government agencies from experiencing similar investment losses. One of those bills was SB 564 (Government Code 53646) which required the annual approval of a formal investment policy by the legislative body at a public meeting.

Discussion

The City of Concord's investment policy incorporates best investment practices as recommended by the Association of Public Treasurers of the US and Canada (APT US&C) while meeting or exceeding the requirements of SB 564. The Policy has been reviewed by the City's external auditors and received APT US&C certification. In the past year, there have been no legislative changes requiring revisions to the Statement of Investment Policy for FY 2009/2010.

Fiscal Impact

Approval of the City of Concord and Redevelopment Agency Investment Policy will have no fiscal impact.

Alternative Courses of Action

Approval of the Investment Policy by the Legislative body is required by law. However, the Council/Agency can request alterations be made to any section as long as the revisions meet the requirements of the State Code.

Recommendation for Action

Staff recommends the City Council and Redevelopment Agency approve the Investment Policy.

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Attachment #1: City of Concord and Concord Redevelopment Agency Investment Policy FY 2009-10

CITY OF CONCORD AND
CONCORD REDEVELOPMENT AGENCY
INVESTMENT POLICY
2009/10

1.0 POLICY

It is the policy of the City of Concord ("City") and the Concord Redevelopment Agency ("Agency", which with the City shall be referred to herein collectively as the "City") to invest public funds in a manner which provides for safety of principal while providing sufficient liquidity to cover the City's short and long term needs. All investment activity will conform to the California Government Code, Sections 53601 through 53659.

In accordance with Section 53646 of the California Government Code, the Treasurer will annually render to the City Council a statement of investment policy.

2.0 SCOPE

This investment policy applies to all financial assets of the City and Agency as accounted for in the City of Concord's Comprehensive Annual Financial Report. Policy statements included in this document focus on the City's pooled funds, but will also apply to all other funds under the Treasurer's control unless specifically exempted by statute or ordinance. This policy includes, but is not limited to the following funds:

a. General Fund
b. Agency Fund
c. Enterprise Funds
d. Capital Project Funds
e. Debt Service Funds
f. Internal Service Funds
g. Special Revenue Funds
h. Any new funds created by the City Council

This policy specifically exempts any City or Agency bond proceed funds in the possession of a trustee or fiscal agent. These bond proceeds shall be invested in accordance with the requirements and restrictions outlined in the bond documents.

3.0 PRUDENCE

All persons authorized to make investment decisions for the City of Concord are trustees and therefore fiduciaries subject to the prudent investor standard.

The standard of prudence to be used by City of Concord fiduciaries is the "Prudent Investor" Standard found in the California Government Code Section 53600.3 and shall be applied in the context of managing the overall portfolio.
The Treasurer and other investment employees, acting within the intent and scope of the Investment Policy and other written procedures, and exercising due diligence, shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely manner and appropriate action is taken to control adverse developments.

4.0 OBJECTIVE

The objective of the investment portfolio is to meet the City's short and long-term cash flow needs. To achieve this objective, the portfolio will be structured to provide, in priority order, safety of principal, liquidity and return on investment.

4.1 Safety

Safety of principal is the foremost objective of the City of Concord. All investments of the City shall be undertaken in a manner that ensures the preservation of capital in the overall portfolio. Each investment transaction shall seek to ensure that capital losses are avoided, whether from issuer default, broker/dealer default, or erosion of market value. The City shall seek to preserve principal by mitigating the two types of risk: credit risk and market risk.

4.1.1 Credit Risk

Credit risk is the risk of loss due to failure of the issuer to repay an obligation and shall be mitigated by investing in only the highest quality credits and by diversifying the investment portfolio so that the failure of any one issuer would not unduly harm the City's cash flows.

4.1.2 Market Risk

Market risk is the risk of market value fluctuations due to overall changes in the general level of interest rates and shall be mitigated by structuring the portfolio so that securities mature at the same time major cash flows occur, eliminating the need to sell securities prior to their maturity; and by prohibiting the taking of short positions, that is, selling securities the City does not own. It is explicitly recognized herein, however, that in a diversified portfolio, occasional measured losses are inevitable and must be considered within the context of overall investment return.

4.2 Liquidity

The City's investment portfolio will be structured to provide sufficient liquidity to meet the operating requirements of the City of Concord.

4.3 Return on Investment

State law requires that the objective of return on investment be subordinate to the objectives of safety and liquidity. Therefore, investment employees shall seek to achieve a return on the funds under their control throughout all economic cycles, taking into consideration the City of Concord's investment risk constraints and cash flow requirements.

5.0 DELEGATION OF AUTHORITY

Pursuant to Section 53601 of the California Government Code, the City Council as the legislative body of the City of Concord has primary responsibility for the investment of surplus monies or monies held in sinking funds, in the City treasury. As authorized under Section 53607 of the California Government Code, the City Council hereby delegates its authority to invest or reinvest the funds of the City, and to sell or exchange securities so purchased, to the City Treasurer who shall assume full responsibility for all such transactions until such time as this delegation of authority may be revoked by the City Council.

Within the Finance Department, the responsibility of day-to-day treasury activities and investment of City funds is delegated by the City Treasurer to the Treasury Manager. In the absence of the Treasury Manager, the Treasury Technician, and the Treasury Account Clerk III, are deputized to act on his/her behalf. Investments made by the Treasury Technician and the Account Clerk III will be restricted to the State Pool (LAIF). The City Treasurer shall establish investment policy guidelines in writing within which the Treasury Manager shall operate day-to-day investment activities. Delegation of Authority will not remove or abridge the Treasurer's investment responsibility.

6.0 ETHICS AND CONFLICT OF INTEREST

In accordance with California Government Code Sections 1090 et seq. and 87100 et seq., elected officials, officers and employees of the City will refrain from any activity that could conflict with the proper execution of the investment program or which could impair their ability to make impartial investment decisions. In addition, these same employees are prohibited from undertaking personal investment transactions with any individual with whom City business is conducted.

7.0 AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS

The City of Concord shall transact business only with commercial banks, savings and loans, and investment securities dealers. The dealers must be primary dealers regularly reporting to the Federal Reserve Bank of New York or regional dealers that qualify under the Securities and Exchange Commission Rule 15C3-1 (uniform net capital rule). Selection of financial institutions and broker/dealers authorized to do business with the City shall be at the sole discretion of the City Treasurer. The Treasurer will maintain a list of financial institutions authorized to provide investment services to the City.

All financial institutions and broker/dealers who desire to become qualified bidders for investment transactions must supply the Treasurer with audited financial statement from the three most recent years, at least three references from other California Local agencies, a completed Broker/dealer questionnaire and a statement certifying that the institution has reviewed the California Government Code Section 53600 et seq. and the City's Investment Policy. The Treasurer shall determine if the Financial Institutions are adequately capitalized, make markets in securities appropriate to the City's needs and are recommended by other local agency portfolio managers.

The Treasurer will conduct an annual review of the financial condition of all qualified institutions. Additionally, their current financial statements are required to be on file.

8.0 AUTHORIZED INVESTMENTS

The City is authorized by California Government Code Section 53600 et seq. to invest in the following types of securities:

8.1 **United States Treasury Bills, Bonds, and Notes,** or those for which the full faith and credit of the United States are pledged for the payment of principal and interest. There is no limitation as to the percentage of the portfolio that can be invested in this category. There is a five-year maximum term.

8.2 **Obligations issued by United States Government Agencies** such as, but not limited to the Federal Farm Credit Bank (FFCB), the Federal Home Loan Bank (FHLB), the Federal Home Loan Mortgage Corporation (FHLMC), the Federal National Mortgage Association (FNMA), the Student Loan Marketing Association (SLMA), the Government National Mortgage Association (GNMA) and the Tennessee Valley Authority (TVA). United States Government Agency securities with call features are also authorized. There is no limitation as to the percentage of the portfolio that can be invested in this category. There is a five-year maximum term.

8.3 Bills of exchange or time drafts drawn on and accepted by a commercial bank, otherwise known as **Banker's Acceptances.** Purchases in this category may not exceed 180 days to maturity or 30% of the cost value of the portfolio.

8.4 **Commercial Paper** of prime quality and ranked P1 by Moody's Investor Services, A1 by Standard and Poor's or F1 by Fitch Financial Services Inc.and issued by a domestic corporation having assets in excess of $500 million and having an "A" or better rating on its long term debt as provided by Moody's, Standard and Poor's or Fitch. Purchases of eligible commercial paper may not exceed 270 days to maturity. Purchases of commercial paper may not exceed 25 percent of the cost value of the portfolio nor represent more than 10 percent of the outstanding paper of an issuing corporation.

Total combined corporate debt (Commercial Paper and Medium Term Notes) may not exceed 30% of the cost value of the portfolio.

8.5 **Negotiable Certificates of Deposit** issued by a nationally or state-chartered bank or a state or federal savings institution. Securities eligible for purchase in this category shall be rated "A" or better by Moody's, Standard and Poor's or Fitch. Purchases of Negotiable Certificates of Deposit shall not exceed 30 percent of the cost value of the portfolio nor exceed a five-year term.

8.6 **Medium Term Notes (MTNs)** issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States. MTNs eligible for investment in this category must be rated "A" or better by Moody's, Standard and Poor's or Fitch. Investments in this category will be limited to a five-year maximum maturity and may not exceed 30 percent of the cost value of the portfolio.

Total combined corporate debt (Commercial Paper and Medium Term Notes) may not exceed 30% of the cost value of the portfolio.

8.7 Shares of beneficial interest issued by diversified management companies that are **Money Market Funds** registered with the Securities and Exchange Commission under the Investment Company Act of 1940. These funds must either have attained the highest rating/ranking by at least two of the three largest nationally recognized rating services or have retained an investment advisor registered with the Securities and Exchange Commission with not less than five year's experience managing money market mutual funds with assets under management in excess of five hundred million dollars ($500,000,000).

Investments in this category will not exceed 5 percent of the portfolio and there is no final maturity.

8.8 State Pool – **Local Agency Investment Fund (LAIF).** This fund was established by the State Treasurer for the benefit of Local agencies under California Government Code Section 16429.1. The City may invest in the LAIF up to the maximum amount permitted by State law.

8.9 **Time Certificates of Deposit** collateralized in accordance with the California Government Code Sections 53652 and 53653, may be purchased by the City from banks or savings and loan associations. Purchases in this category will not exceed 5 years to maturity or 30 percent of the cost value of the portfolio. Purchases in a single institution will not exceed 10 percent of the cost value of the portfolio.

8.10 **Derivative Securities** are those securities that derive their value from another asset or index. Investments in derivative securities will be made using the Prudent Investor Rule and will be limited to federal agency callable issues.

8.11 **Prohibited Investments.** Investments not described herein are ineligible investments. The City shall not invest any funds in inverse floaters, range notes, or interest only strips that are derived from a pool of mortgages in accordance with California Government Code Section 53601.6. With the exception of callable agencies, any security that derives its value from another asset or index is prohibited. In addition, the City shall not invest any funds in any security that could result in zero interest accrual if held to maturity.

9.0 INVESTMENT POOLS/MUTUAL FUNDS

A thorough investigation of any investment pool or money market mutual fund is required prior to investing City funds. A due diligence review will be performed on all money market mutual funds and pooled investment funds on a continued basis.

As outlined in section 8.7 of this policy, investments in mutual funds are restricted to money market mutual funds and must meet the experience and asset requirements as stated. Treasury staff will continually monitor the funds to ensure the maintenance of those ratings/requirements.

Reports on the performance of the Pooled Money Investment Account/LAIF can be found on the California State Treasurer's web site as well as the Investment Board report, historical rates/costs and market valuations. These reports should be reviewed each month as part of the due diligence review.

10.0 COLLATERALIZATION

California Government Code, Sections 53652 et seq., specifies the types and levels of collateral for public funds on deposit above the FDIC insurance amounts. These collateral requirements apply to both active bank deposits (checking and savings accounts) and inactive bank deposits (non-negotiable certificates of deposit) and must be maintained for all the City's bank deposits

11.0 SAFEKEEPING AND CUSTODY

All securities held by the City of Concord shall be held in safekeeping by a third party bank trust department acting as agent for the City under the terms of the custody agreement executed by the bank and the City, and shall be evidenced by safekeeping receipts. All securities will be received and delivered using standard delivery-versus-payment (DVP) procedures. Investments in the State Pool or money market mutual funds are undeliverable and are not subject to delivery or third party safekeeping.

12.0 DIVERSIFICATION

The City of Concord will diversify its portfolio by investment type, issuer, maturity dates and broker/dealer. For purposes of diversification, LAIF accounts will not be aggregated. Limits for security types are set forth in Section 8.0 of this document.

13.0 MAXIMUM MATURITIES

The City of Concord will attempt to match its investments with anticipated cash flow requirements whenever possible. The maximum maturity of any one security, unless otherwise restricted by the California Government Code, is limited to five years. The portfolio's weighted average maturity shall be limited to three years.

14.0 INTERNAL CONTROLS

The City Treasurer has developed a system of internal controls to ensure compliance with investment policies and procedures of the City and Redevelopment Agency of the City of Concord and the California Government Code.

15.0 REPORTING

On a monthly basis, the Treasurer shall render a report to the City Council. The report shall be submitted within 30 days of the end of the month covered by the report and shall include the type of investment, issuer, maturity date, par and cost/book values of all securities, investments and monies held by the City of Concord. It shall also include the rate of interest, the current market value as of the report date and the source of the valuation. The report shall state compliance of the portfolio to the Investment policy as well as the California Government Code and it shall state the City's ability to meet its estimated expenditures for the next six months.

16.0 INVESTMENT POLICY ADOPTION

The City of Concord's investment policy shall be rendered to and adopted by the City Council annually as required by California Government Code 53646.

17.0 GLOSSARY

AGENCIES: Federal agency securities and/or Government sponsored enterprises.

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

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

CERTIFICATE OF DEPOSIT (CD): A time deposit with a specific maturity evidenced by a certificate. Time certificates of deposit are collateralized in accordance with the State code. Large-denomination CD's are typically negotiable and non-collateralized.

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.

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

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

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

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

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

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

FEDERAL HOME LOAN BANKS (FHLB): Government sponsored wholesale banks (currently 12 regional banks) which lend funds and provide correspondent banking services to member commercial banks, thrift institutions, credit unions and insurance companies. The mission of the FHLB is to liquefy the housing related assets of its members who must purchase stock in their district Bank.

FEDERAL NATIONAL MORTGAGE ASSOCIATION (FNMA or Fannie Mae)): FNMA, like GNMA was chartered under the Federal National Mortgage Association Act in 1938. FNMA is a federal corporation working under the auspices of the Department of Housing and Urban Development (HUD). It is the largest single provider of residential mortgage funds in the United States. Fannie Mae, as the corporation is called, is a private stockholder-owned corporation. The corporation's purchases include a variety of adjustable mortgages and second loans, in addition to fixed-rate mortgages. FNMA's securities are also highly liquid and are widely accepted. FNMA assumes and guarantees that all security holders will receive timely payment of principal and interest.

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

GOVERNMENT NATIONAL MORTGAGE ASSOCIATION (GNMA or Ginnie Mae): Securities influencing the volume of bank credit guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loan associations, and other institutions. Security holder is protected by full faith and credit of the US Government. Ginnie Mae securities are backed by the mortgages, including FHA and VA mortgages. The term "pass-throughs" is often used to describe Ginnie Maes.

ISSUER: A legal entity that has the power to issue and distribute securities. Issuers include corporations, municipalities, foreign and domestic governments and their agencies, and investment trusts.

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

POOLED MONEY INVESTMENT FUND (LAIF): The aggregate of all funds from political subdivisions that are placed in the custody of the County or State Treasurer for investment and reinvestment. The State of California's pool is known as the Local Agency Investment Fund, or LAIF.

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 (bills, commercial paper, bankers' acceptances, etc.) are issued and traded.

PORTFOLIO: Collection of securities and investments held by an investor.

PRIMARY DEALER: A group of government securities dealers who submit daily reports of market activity 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.

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 custody state. In other states, the trustee may invest in a security if it is one which would be bought by a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital.

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.

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

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

SEC RULE 15C301: See Uniform Net Capital Rule.

TREASURY 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 BONDS: Long-term coupon-bearing US Treasury securities issued as direct obligations of the US Government and having initial maturities of more than 10 years.

TREASURY NOTES: Medium-term coupon-bearing US Treasury securities issued as direct obligations of the US Government and having initial maturities from two to 10 years.

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

YIELD: The rate of annual income return on an investment, expressed as a percentage: (a) Income Yield is obtained by dividing the current dollar income by the current market price for the security; (b) Net Yield or Yield to Maturity is the current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond.