PURPOSE
This policy sets forth the procedural regulations for investing surplus funds. The intent of the Investment Policy of the City of West Sacramento is to define the parameters within which funds are to be managed.

POLICY
In methods, procedures, and practices, the policy formalizes the framework for the City's investment activities that must be exercised to ensure effective and judicious fiscal and investment management of the City's funds. The guidelines are intended to be broad enough to allow the investment officer to function properly within the parameters of responsibility and authority, yet specific enough to safeguard the investment assets.

PROCEDURE
A. SCOPE

This policy applies to the investment of surplus operating and capital funds and proceeds from certain bond issues. It conforms to Government Finance Officers Association’s Sample Investment Policy (GFOA Revised 2011).

1. Pooling of Funds: Except for cash in certain restricted and special funds, the City will consolidate cash balances from all funds to maximize investment earnings. Investment income will be allocated to the various funds based on their respective participation and in accordance with generally accepted accounting principles.

B. GENERAL OBJECTIVES

The primary objectives, in priority order, of investment activities shall be safety, liquidity, and yield.

1. Safety: Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk and interest rate risk.

   a. Credit Risk: The City will minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

      • Limiting investments to the safest types of securities.
      • Prequalifying the financial institutions, broker/dealers, intermediaries, and advisors with which the City will do business.
Administrative Policy IV-C-2

Investment Policy
(continued)

- Diversifying the investment portfolio so that potential losses on individual securities will be minimized.

b. Interest Rate Risk: The City will minimize the risk that the market value of securities in the portfolio will fall due to changes in general interest rates, by:

- Structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity.

- Investing operating funds primarily in shorter-term securities, money market mutual funds, or similar investment pools.

2. **Liquidity**: The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by structuring the portfolio so that securities mature concurrent with cash needs to meet anticipated demands (static liquidity). Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets (dynamic liquidity). A portion of the portfolio also may be placed in money market mutual funds or local government investment pools which offer same-day liquidity for short-term funds.

3. **Yield**: The 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 liquidity needs. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core of investments are limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed. Securities shall not be sold prior to maturity with the following exceptions:

- A security with declining credit may be sold early to minimize loss of principal.

- A security swap would improve the quality, yield, or target duration in the portfolio.

- Liquidity needs of the portfolio require that the security be sold.

C. **STANDARDS OF CARE**

1. **Prudence**: The standard of prudence to be used by investment officials shall be the “prudent person” standard (California Government Code section 53600.3) and shall be applied in the context of managing an overall portfolio. Investment officers acting in accordance with written procedures and this investment policy and exercising due diligence shall be relieved of personal responsibility for an individual security’s credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and the liquidity and the sale of securities are carried out in accordance with the terms of this policy.

   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.

2. **Ethics and Conflicts of Interest**: Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with the proper execution and management of the investment program, or that could impair their ability to
make impartial decisions. Employees and investment officials shall disclose any material interests in financial institutions with which they conduct business. They shall further disclose any personal financial/ investment positions that could be related to the performance of the investment portfolio. Employees and officers shall refrain from undertaking personal investment transactions with the same individual with whom business is conducted on behalf of the City.

3. *Delegation of Authority:* Authority to manage the investment program is granted to the Director of Finance/City Treasurer, hereinafter referred to as investment officer, and derived from Ordinance 87-12. Responsibility for the operation of the investment program is hereby delegated to the investment officer, who shall act in accordance with established written procedures and internal controls for the operation of the investment program consistent with this investment policy. Procedures should include references to: safekeeping, delivery vs. payment, investment accounting, repurchase agreements, wire transfer agreements, and collateral/depository agreements. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the investment officer. The investment officer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

D. SAFEKEEPING AND CUSTODY

1. *Authorized Financial Dealers and Institutions:* A list will be maintained of financial institutions authorized to provide investment services. In addition, a list also will be maintained of approved security broker/dealers selected by creditworthiness (e.g., a minimum capital requirement of $10,000,000 and at least five years of operation). These may include “primary” dealers or regional dealers that qualify under Securities and Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule).

   All financial institutions and broker/dealers who desire to become qualified for investment transactions must supply the following as appropriate:

   • Audited financial statements.
   • Proof of National Association of Securities Dealers (NASD) certification.
   • Proof of state registration.
   • Completed broker/dealer questionnaire.
   • Certification of having read and understood and agreeing to comply with the City’s investment policy.
   • Evidence of adequate insurance coverage.

   An annual review of the financial condition and registration of qualified financial institutions and broker/dealers will be conducted by the investment officer.

   From time to time, the investment officer may choose to invest in instruments offered by minority and community financial institutions. In such instances, a waiver to the criteria under Paragraph 1 may be granted. All terms and relationships will be fully disclosed prior to purchase and will be reported to the appropriate entity on a consistent basis and should be consistent with state or local law. These types of investment purchases should be approved by the appropriate legislative or governing body in advance.
2. **Internal Controls**: The investment officer is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the City are protected from loss, theft or misuse. Specifics for the internal controls shall be documented in an investment procedures manual that shall be reviewed and updated periodically by the Investment Officer. An example of such a procedure would include the requirement that the Director of Finance approve trades transacted by other authorized personnel. The internal control structure shall be designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived and (2) the valuation of costs and benefits requires estimates and judgments by management.

Accordingly, the investment officer shall establish a process for an annual independent review by an external auditor to assure compliance with policies and procedures. The internal controls shall address the following points:

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

3. **Delivery vs. Payment**: All trades where applicable will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible financial institution prior to the release of funds. Securities will be held by a third-party custodian as evidenced by safekeeping receipts. The only exception to the foregoing shall be depository accounts and securities purchase made with: Local Agency Investment Fund (LAIF), California Asset Management Program, time certificates of deposit and money market mutual funds, since the purchased securities are not deliverable.

4. **Third-Party Safekeeping**: Securities will be held by an independent third-party safekeeping institution selected by the City. All securities will be evidenced by safekeeping receipts in the City’s name. The safekeeping institution shall annually provide a copy of its most recent report on internal controls – Service Organization Control Reports (formerly 70, or SAS 70) prepared in accordance with the Statements of Standards for Attestation Engagements (SSAE) No. 16 (effective June 15, 2011).

E. **SUITABLE AND AUTHORIZED INVESTMENTS**

1. **Investment Types**: Investments shall be placed to conform to those allowable under the State of California Government Code section 53600 and 53635. Consistent with the GFOA
Policy Statement and Local Laws Concerning Investment Practices, the following investments will be permitted by this policy and are those defined by state and local law where applicable. If additional types of securities are approved for investment by public funds by state statute, they will not be eligible for investment by the City until this Policy has been amended and the amended version adopted by the City Council. Typical types of authorized securities are:

- U.S. Treasury and other government obligations that carry the full faith and credit guarantee of the United States for the payment of principal and interest;
- Federal Agency or U.S. Government Sponsored Enterprises (GSE) obligations, participations or other instruments;
- Banker’s Acceptances;
- Federally insured time deposits (non-negotiable certificates of deposit) in state or federally chartered banks, savings and loans, or credit unions, provided that the amount per institution is limited to the maximum covered under federal insurance;
- Negotiable certificates of deposit;
- Commercial paper, rated in the highest tier (e.g., A-1, P-1, F-1, or D-1 or higher) by a nationally recognized statistical rating organization;
- Corporate bonds;
- Investment-grade obligations of state, provincial and local governments and public authorities;
- Fully collateralized Repurchase Agreements collateralized in compliance with this Policy, governed by SIFMA Master Repurchase Agreement and with a maximum maturity. Capital project funds may be invested in a single flex repurchase agreement with a maximum stated maturity that shall be matched to the expenditure plan;
- SEC registered money market mutual funds; and
- Local government investment pools.

2. **Collateralization**: Acceptable collateral for bank deposits and repurchase agreements shall include only:

- Obligations of the U.S. Government, its agencies and GSEs, including mortgage backed securities.
- Obligations of any state, city, county or authority rated at least AA (or equivalent) by two nationally recognized statistical rating organizations.

F. INVESTMENT PARAMETERS

1. **Diversification**: The investments shall be diversified by:

- limiting investments to avoid over-concentration in securities from a specific issuer or business sector (excluding U.S. Treasury securities),
- limiting investment in securities that have higher credit risks,
• investing in securities with varying maturities, and

• continuously investing a portion of the portfolio in readily available funds such as local government investment pools (LGIPs), money market funds or overnight repurchase agreements to ensure that appropriate liquidity is maintained in order to meet ongoing obligations.

2. Maximum Maturities: To the extent possible, the City shall 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 years from the date of purchase or in accordance with state and local statutes and ordinances. The City shall adopt weighted average maturity limitations (which often range from 90 days to three years), consistent with the investment objectives.

Reserve funds and other funds with longer-term investment horizons may be invested in securities exceeding five years if the maturity of such investments are made to coincide as nearly as practicable with the expected use of funds. The intent to invest in securities with longer maturities shall be disclosed in advance in writing to the legislative body (per Government Code Section 53601).

Because of inherent difficulties in accurately forecasting cash flow requirements, a portion of the portfolio should be continuously invested in readily available funds such as LGIPs, money market funds, or overnight repurchase agreements to ensure that appropriate liquidity is maintained to meet ongoing obligations.

G. INVESTMENT STRATEGIES:

The investment program shall seek to augment returns consistent with the intent of this policy, identified risk limitations and prudent investment principles. These objectives will be achieved by use of the following strategies:

The source of and purpose for surplus funds determines the goal to be accomplished by the strategy. Bond proceeds, for example, typically have three purposes: reserve funds, project funds, and debt service funds. The goal and corresponding investment strategy is different for each, as follows:

• Reserve Funds. The goal is to have these funds available in case of default while minimizing negative arbitrage. The strategy is to call for competitive bids for long-term investment agreements with a call provision for default or redemption from AAA-rated limitations.

• Project Funds. The goal is to maintain purchasing power. The strategy, assuming a normal yield curve, is to match investment agreement maturities with construction draw schedules. Funds needed within 12 months are currently placed in an AAA-rated mutual fund of U.S. Treasury Securities.

• Debt Service Funds. The goal is to maintain liquidity. Generally, funds are placed in a money market mutual fund related investment category.

Surplus funds in the City pool come from a mixed bag of services for a wide variety of purposes. This blend of funds leads to the general investment goal of earning an appropriate yield consistent with the City’s high standards for safety and liquidity.
A simple investment strategy for accomplishing this goal is to invest totally in the State’s LAIF. In a normal yield curve environment, LAIF can generally outperform other investments because it invests for a longer term.

This advantage holds when the yield curve begins to flatten, but becomes a disadvantage when the curve increases its slope.

This relationship between LAIF and a changing yield curve suggests the slightly more complex investment strategy of playing LAIF against the market for greater yields when interest rates are rising.

H. INVESTMENT PERFORMANCE

In a normal financial market, the yield curve shows greater rewards for longer terms.

Since the shortest-term investment strategy (for surplus funds in the City pool) is to play the market against LAIF, the minimum acceptable return ought to be greater than LAIF. In addition, the quarter to date LAIF apportionment rate, the three-month U.S. Treasury Bill and the two-year U.S. Treasury Note shall also be considered benchmarks of the City’s portfolio performance.

Accordingly, LAIF and U.S. Treasuries will be the benchmark for evaluating performance.

I. REPORTING

1. *Methods:* The investment officer shall prepare an investment report at least quarterly, including a management summary that provides an analysis of the status of the current investment portfolio and the individual transactions executed over the last quarter. This report shall include the type of investment, issuer, date of maturity, and par and dollar amount invested on all securities, investments and moneys held by the City. The report shall also include a current market value as of the date of the report. It shall state compliance of the portfolio to the statement of investment policy or manner in which the portfolio is not in compliance. Finally, the report shall include a statement denoting the ability of the local agency to meet its pool’s expenditure requirements for the next six months or provide an explanation as to why sufficient money shall, or may, not be available. Once a year, the statement of investment policy shall be included in the report.

2. *Performance Standards:* The investment portfolio will be managed in accordance with the parameters specified within this policy. The portfolio should obtain a market average rate of return during a market/economic environment of stable interest rates. A series of appropriate benchmarks shall be established against which portfolio performance shall be compared on a regular basis.

3. *Marking to Market:* The market value of the portfolio shall be calculated at least quarterly and a statement of the market value of the portfolio shall be issued at least quarterly. This will ensure that review of the investment portfolio, in terms of value and price volatility, has been performed consistent with the GFOA Recommended Practice on “Mark-to-Market Practices for State and Local Government Investment Portfolios and Investment Pools.” In defining market value, considerations should be given to the GASB Statement 31 pronouncement.

4. *Annual Reports:* The investment policy shall be reviewed at least annually within 120 days of the end of the 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. A comprehensive annual report shall be presented in conjunction with the investment policy review. This report shall include comparisons of City’s return to the City’s benchmark return, shall suggest policies and improvements that might enhance the investment program, and shall include an investment plan for the coming year.

5. **Annual Audit:** Management shall establish an annual process of independent review by the external auditor to assure compliance with internal controls. Such audit will include tests deemed appropriate by the auditor.

J. **POLICY CONSIDERATIONS**

1. **Exemption:** Any investment currently held as of October 15, 2014 that does not meet the guidelines of this policy shall be exempted from the requirements of this policy. At maturity or liquidation, such monies shall be reinvested only as provided by this policy.

2. **Amendments:** This policy shall be reviewed on an annual basis. Any changes must be approved by the investment officer and City Council, as well as the individuals charged with maintaining internal controls.

K. **GLOSSARY OF TERMS**

**US Treasury Obligation:** Direct obligations of the United States Treasury whose payment is guaranteed by the United States.

**GSE Obligations:** US Government Agencies, Government Sponsored Enterprises (GSEs), Corporations or Instrumentalities of the US Government — Federal Instrumentality Securities include, but are not limited to Federal Nation Mortgage Association, the Federal Home Loan Mortgage Corporation, Federal Home Loan Banks, and the Federal Farm Credit Bureau.

**TLGP Debt Obligations:** Senior unsecured debt obligations guaranteed by the Federal Deposit Insurance Corporation under the Temporary Liquidity Guarantee Program (TLGP) or other federal government guaranteed programs; Eligible debt obligations must carry the full faith and credit of the United States Government (if allowable).

**Commercial Paper:** Commercial Paper that is rated A1/P1 and has long term bonds which have a minimum rating of AA- by Standard and Poor’s and Aa3 by Moody’s.

**Banker’s Acceptances:** Banker’s acceptances, if the banker’s acceptances are (i) guaranteed by, and carried on the books of, a qualified financial institution; (ii) eligible for discount by the Federal Reserve System; and (iii) issued by a qualified financial institution whose short-term letter of credit rating is rated in the highest category by one or more nationally recognized statistical rating organizations.

**Repurchase Agreements:** An agreement with an approved broker/dealer that provides for sell and simultaneous purchase of an allowable collateral security. The difference in the sales and purchase price is the earning rate on the agreement. A master repurchase agreement must be in place with the approved broker dealer.

**Corporate Indebtedness:** Corporate Indebtedness that has a minimum long-term debt rating of AA- rated by Standard and Poor’s and a Aa3 rating by Moody’s and must be rated on the settlement date P-1 or Aa or better by Moody’s Investors Service or A-1 or AA or better by Standard and Poor’s Corporation or equivalent rating by any nationally recognized statistical rating organization.
Local Government Investment Pool: State treasurer's local short-term investment fund up to the statutory limit per state statute.

Certificates of Deposit/Bank Deposit/Savings Accounts: Time deposits open accounts, certificates of deposit and savings accounts in insured institutions as defined in state statute, in credit unions as defined in state statute, or in federal credit unions, if the institution or credit union maintains a head office or branch in the State of California.

Municipal Obligations: Lawfully issued debt obligations of the agencies and instrumentalities of the State of California and its political subdivisions that have a long-term rating of “A” or an equivalent rating or better or are rated on the settlement date in the highest category for short-term municipal debt by a nationally recognized statistical rating organization.