

**Council Meeting: October 22, 2013****SUBJECT: Adopt the City's Investment Policy for Fiscal Year 2013/14****BACKGROUND**

The City Council adopted a policy governing the investment of City funds on July 30, 1985. This policy has been reviewed and adopted on an annual basis since that time.

**EXISTING POLICY**

The City's Investment Policy requires that it be adopted annually within 120 days of the fiscal year to ensure consistency with the overall objectives of safety, liquidity, and yield, and its relevance to current law and financial and economic trends. A report out on portfolio performance for the preceding fiscal year is also presented to the City Council as part of the annual investment policy review.

**CEQA REVIEW**

N/A.

**DISCUSSION**

Staff invests funds not immediately needed for disbursement. Funds for the City's Deferred Compensation Plan, the City's Retirement Plan, Other Post- Employment Benefits (OPEB) Trust, and debt issuance proceeds are not invested by City staff.

The key provisions of the existing policy are as follows:

1. Safety of principal is the foremost objective of the investment program. The City's portfolio is diversified by type of investment, issuer, and maturity date. Diversification is required in order that potential losses on individual securities do not exceed the income generated from the remainder of the portfolio. All investments in the portfolio are authorized by the investment policy and the City is in compliance with the requirement that all investments be held in safekeeping by a third party bank trust department. The City currently has a contract with Union Bank to provide this service.
2. Liquidity- the portfolio will remain sufficiently liquid to enable the City to meet all operating requirements which might be reasonably anticipated. A schedule of major revenues and expenditures for at least 12 months is maintained in order to determine liquidity needs. Liquidity requirements have been met through utilizing the State's Local Agency Investment Fund (LAIF) and the City's interest bearing bank accounts. Approximately 17% of the portfolio was in LAIF at the end of FY 2012/13.

3. Yield- the portfolio will be maintained with the objectives of safety and liquidity first, and then the objective of obtaining a market rate of return throughout the budgetary and economic cycles, taking into account the City's investment risk constraints and the cash flow characteristics of the portfolio.

The annual report out on portfolio performance for FY 2012/13 includes comparisons of the City's performance compared to the investment policy objectives and a section on compliance with the investment policy. For FY 2012/13, the portfolio yield averaged .60% while the average yield of our benchmark (Treasury securities with an average life similar to our portfolio) was .21%; a difference of .39%.

With yields at historical all-time lows, the City's investment strategy continues to be one of keeping investments short in anticipation of rising interest rates. The average maturity of the portfolio on June 30, 2013 was 442 days. When interest rates increase, investments existing in the portfolio with longer maturities that were purchased when rates were low will experience a decrease in their market value because the interest rate on those investments is less than the current market's interest rate. The strategy is to invest in higher yielding investments when rates rise as opposed to having to wait for low interest bearing investments to mature or sell those investments at a loss so that funds can be reinvested at the higher rate.

#### Proposed Changes to Investment Policy

The City's Investment Policy has been reviewed and certified annually by the Association of Public Treasurers of the United States and Canada (APT US&C) since 1999. Staff will submit the Investment Policy for FY 2013/14 (once approved by Council) to be re-certified. In addition, this year an independent third party review of the City's Investment Policy was conducted by Chandler Asset Management, a firm founded in 1988 that specializes in portfolio management for public agencies in California and has periodically reviewed the City's investment policy in the past. Chandler reviewed the City's Investment Policy for compliance with State law and with best practices. Based on the review, Chandler has proposed several changes to provide the City more flexibility while maintaining the key provisions of the Policy. Attached to this Report is a strikeout version of the proposed changes, which are summarized below:

Currently, only regional broker/dealers headquartered in California are authorized to do business with the City. Chandler recommends providing more flexibility to the City by allowing regional broker/dealers not headquartered in California to do business with the City. City staff will continue to follow the current practice of reviewing audited financial statements and broker/dealers files through the Financial Industry Regulatory Authority (FINRA) as well as perform reference checks.

The current policy requires any broker/dealer to certify that they will comply with the investment policy. Requiring a compliance certification of broker/dealers would require that they have real-time access to the City's portfolio to ensure that they don't offer an investment that may cause the City to exceed the allowable percentage for an investment type or issuer. This has limited the number of broker/dealers available to the City. Chandler recommends that the policy be amended to require broker/dealers to

certify that they have reviewed the City's Investment Policy to ensure that they are aware of the investments that are prohibited.

Chandler is recommending that the maturity for federally insured Bank Deposits and Negotiable Certificates of Deposit be extended from 180 days to 5 years and that the maximum maturity for commercial paper be extended from 180 days to 270 days. Longer maturities for these investments is permitted by State law and allows more flexibility to the City.

Ratings on Bank Deposits which are fully collateralized, which means the issuer has posted collateral to cover the investment, are not required by State law and Chandler is proposing that the rating requirement for this investment type be deleted from the Investment Policy.

Chandler is recommending that the City only invest in mortgage pass-through securities and asset-backed securities that have an issuer debt rating of A or higher in addition to the current requirement of a AAA issue rating and that all Municipal Securities have at least an A rating.

Two new investment alternatives are proposed to be added to the Investment Policy:

- 1) Certificate of Deposit (CD) Placement Service - this investment type will allow the City to utilize a member of a financial network, such as the CDARS Promontory Interfinancial Network, to place the City's funds into CDs issued by other members of the network. This occurs in increments lower than the \$250,000 insurance limit so that both principal and interest are covered by insurance. Currently, if the City wants to purchase an insured CD, the City has to contact each bank individually and deposit an amount under \$250,000. This investment type will allow the City to deposit a much larger amount and the member bank places the funds with the other members on behalf of the City. Although this is a new investment type, the maximum percentage that can be invested is proposed to be combined with Negotiable Certificates of Deposit and may not exceed 30% of the total portfolio.
- 2) Joint Powers Authority (JPA) Pools - this change will allow flexibility to the City to invest up to 10% of the investment portfolio in a pool. The pool must be managed by an investment advisor with at least five years of local agency investment experience that has assets under management in excess of \$500,000,000.

The proposed Investment Policy also allows the City to employ an investment advisor to invest all or a portion of the City's cash. This change provides additional options to the City for management of the City's investment portfolio. The advisor must be registered under the Investment Advisers Act of 1940.

The proposed Investment Policy requires that a monthly transaction report be provided to the City Council. Although staff has been providing this report, this requirement was not called out in the Investment Policy.

**FISCAL IMPACT**

There is no fiscal impact associated with adoption of the Investment Policy. Interest earnings for FY 2012/13 for all City funds totaled \$1,487,129.

**PUBLIC CONTACT**

Public contact was made by posting the Council agenda on the City's official-notice bulletin board outside City Hall, at the Sunnyvale Senior Center, Community Center and Department of Public Safety; and by making the agenda and report available at the Sunnyvale Public Library, the Office of the City Clerk and on the City's Web site.

**ALTERNATIVES**

1. Adopt the attached Investment Policy for FY 2013/14 as presented.
2. Adopt the attached Investment Policy for FY 2013/14 with changes as proposed by the City Council.

**RECOMMENDATION**

Staff recommends Alternative 1, adopt the attached Investment Policy for FY 2013/14 as presented. Staff is in agreement on these proposed changes as they will provide greater flexibility for investing the City's idle funds.

Reviewed by:

Grace K. Leung, Director, Finance  
Prepared by: Therese Balbo, Treasury Manager

Approved by:

Gary M. Luebbbers  
City Manager

**Attachments**

- A. Proposed Investment Policy for FY 2013/14 (Strikeout version)

# CITY OF SUNNYVALE

INVESTMENT ~~AND CASH MANAGEMENT~~ POLICY

FY ~~2012/2013~~ 2013/14

# CITY OF SUNNYVALE

## Investment ~~and Cash Management~~ Policy

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## I. INVESTMENT PHILOSOPHY Purpose and Investment Philosophy

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### A. Policy

The City establishes investment policies that meet its current investment goals. This policy is intended to establish objectives and criteria for the investment of the City's temporarily idle funds and ~~for funds managed by the City's Redevelopment Agency, and for the City's Redevelopment Successor Agency and~~ to provide guidelines for the City's cash management system.

### B. Purpose

This policy is set forth by the City of Sunnyvale (City) for the following purposes:

1. To establish a clear understanding for the City Council, City management, responsible employees, citizens and third parties of the objectives, policies and guidelines for the investment of the City's temporarily idle funds;
2. To offer guidance to investment staff on the investment of City funds; and
3. To establish a basis for evaluating investment results.

### C. Objectives

The City's cash management system shall be designed to accurately monitor and forecast expenditures and revenues, to enable the City ~~and its Redevelopment Agency~~ to invest funds to the fullest extent possible.

Idle funds of the City ~~of Sunnyvale~~ shall be invested in accordance with principles of sound treasury management and in accordance with the provisions of California Government Code Section 53600 et seq., the City Charter, the ~~Sunnyvale City's~~ Municipal Code and this policy.

The objectives of ~~Sunnyvale's the City's~~ investment program are, in order of priority:

1. Safety – Safety of principal is the foremost objective of the investment program. Investments of the City ~~of Sunnyvale~~ shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. To attain this objective, diversification is required in order that potential losses on individual securities do not exceed the income generated from the remainder of the portfolio.

2. Liquidity – The City’s investment portfolio will remain sufficiently liquid to enable the City ~~of Sunnyvale~~ to meet all operating requirements which might be reasonably anticipated.
3. Return on Investment –The City’s investment portfolio shall be designed with the objective of attaining the safety and liquidity objectives first, and then attaining a market rate of return throughout the budgetary and economic cycles, taking into account the ~~City of Sunnyvale’s~~ City’s investment risk constraints and the cash flow characteristics of the portfolio.

#### **D. Prudence Standard of Care – Prudent Investor**

The governing body of the City ~~of Sunnyvale~~, and any staff members authorized to make investment decisions on behalf of the City are trustees and therefore fiduciaries subject to the prudent investor standard. When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the City, that a prudent person acting in a like capacity and familiar with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the City. Within the limitations of this section and considering individual investments as part of an overall strategy, investments may be acquired as authorized by law.

The ~~Finance-Treasury~~ Manager (~~Treasury~~) and Director of Finance (or his/her designee) are authorized to manage the investment portfolio and acting within the intent and scope of the investment policy and other written procedures and exercising due diligence, shall be relieved of personal responsibility and liability 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.

#### **E. Ethics and Conflicts of Interest**

Officers and employees involved with 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 ~~Finance-Treasury~~ Manager (~~Treasury~~), and other designated employees are required to file applicable financial disclosures, as required by the Fair Political Practices Commission.

## **II. OPERATIONAL AND PROCEDURAL MATTERS**

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### **A. Scope**

This Investment Policy applies to all funds and investment activities of the City ~~of Sunnyvale~~ with the following exceptions:

1. The City's Deferred Compensation Plan is excluded because it is managed by a third party administrator and invested by individual plan participants;
2. The City participates in the Public Employees Retirement System, and does not manage any retirement funds internally.
3. Proceeds of debt issuance shall be invested in accordance with the general investment philosophy of the City as set forth in this policy; however, such proceeds are invested in accordance with permitted investment provisions of their specific bond indentures.
4. Funds for the Other Post Employment Benefits (OPEB) Trust shall be invested in accordance with the general investment philosophy of the City as set forth in this policy; however, these funds are invested pursuant to California code and the Trust's separate long-term investment policy as approved by Council under the Trust Agreement.

## **B. Authorized Financial Dealers and Institutions**

1. The Director of Finance or his/her designee shall maintain a list of institutions qualified and authorized ~~institutions eligible~~ to transact investment business with the City. Eligible institutions include:
  - a. Primary government dealers as designated by the Federal Reserve Bank;
  - b. Regional broker/dealers ~~headquartered in the State of California~~;
  - c. Nationally or state-chartered banks;
  - d. The Federal Reserve Bank; and
  - e. Direct issuers of securities eligible for purchase by the City.
2. Public deposits shall be made only in qualified public depositories within the State of California as established by State law, or as permitted by Section III.A (4-7). Deposits shall be insured by the Federal Deposit Insurance Corporation, or, to the extent the amount exceeds the insured maximum, shall be collateralized with securities in accordance with state law.
3. A sufficient pool of qualified financial institutions and dealers will be maintained using criteria based on credit worthiness, experience, reference checks, and qualifications under the Securities and Exchange Commission. All broker/dealers who desire to become qualified must be registered with Financial Industry Regulatory Authority (FINRA) and supply the following as appropriate:
  - a. Audited financial statements

- b. Completed broker/dealer questionnaire
  - c. Certification of having ~~read and agreeing to comply with~~reviewed the City's Investment Policy.
4. It is the policy of the City to require competitive bidding for investment transactions. Whenever possible, at least three financial dealers or institutions will be contacted to provide ~~prices~~ price quotations on security purchases and sales.
  5. Selection of financial institutions and broker/dealers used by the City shall be at the sole discretion of the City.

### **C. Delivery vs. Payment**

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

### **D. Safekeeping of Securities**

To protect against potential losses by collapse of individual securities dealers, and to enhance access to securities, interest payments, and maturity proceeds, all securities owned by the City shall be held in safekeeping by a third party bank trust department, acting as agent for the City under the terms of a custody agreement executed by the bank and by the City.

## **III. PERMITTED INVESTMENTS AND GUIDELINES TO ACHIEVE POLICY OBJECTIVES**

### **A. Authorized Investments**

All investments shall be made in accordance with Sections 53600 *et seq.* of the Government Code of California and as described within this Investment Policy. Permitted investments under this policy shall include:

1. **Securities issued by the US Treasury**, ~~provided that:~~
  - a. There shall be no maximum allowable investment in US Treasury securities; and
  - b. As required by Section 53601 of the California Government Code, the City Council hereby grants express authority to the Finance Treasury Manager (~~Treasury~~) to invest in U.S. Treasury securities with final stated maturities up to seven years.

2. **Securities issued and fully guaranteed as to payment by a federal agency or issued by a United States Government Sponsored Enterprise**, provided that:
  - a. No more than 30% of the total portfolio may be invested in federal agencies or government sponsored enterprises of any single issuer; and
  - b. As required by Section 53601 of the California Government Code, the City Council hereby grants express authority to the Treasury Manager to invest in U. S. Agency securities with final stated maturities up to seven years.
  
3. **Banker's acceptances**, provided that:
  - a. ~~They are issued by institutions the short term obligations of which are rated a minimum of P1 by Moody's or A1 by Standard & Poor's (S&P); or, if the short term obligations are unrated, the long term obligations of which are rated a minimum of A by Moody's and S&P; No more than 30% of the total portfolio may be invested in banker's acceptances.~~
  - b. Their maturity does not exceed 180 days; ~~and~~
  - c. ~~No more than 30% of the total portfolio may be invested in banker's acceptances. They are issued by institutions with short term debt obligations rated a minimum of P-1 by Moody's or A-1 by Standard and Poors, or the equivalent by a nationally recognized statistical-rating organization (NRSRO); and~~
  - d. No more than 5% of the total portfolio may be invested per issuer.
  
4. Federally Insured Bank Deposits (Non-negotiable certificates of deposit) in state or federally chartered banks, savings and loans, or credit unions in the state of California provided that:
4. ~~Federally insured time deposits (Non-negotiable certificates of deposit) in California banks with a maximum maturity of 365 days, provided that:~~
  - a. No more than 20% of the total portfolio shall be invested in a combination of federally insured and collateralized time deposits;
  - b. The amount per institution is limited to the maximum covered under federal insurance; and
  - c. Their maturity does not exceed five years .
  
5. Collateralized Bank Deposits (Non-negotiable certificates of deposit) in California banks in excess of insured amounts which are fully collateralized with securities in accordance with California law, provided that: ~~Time deposits (Non-negotiable~~

~~certificates of deposit) in California banks in excess of insured amounts which are fully collateralized with securities in accordance with California law, provided that:~~

- a. ~~No more than 20% of the total portfolio shall be invested in a combination of federally insured and collateralized time deposits and no more than 5% of per issuer; and~~
- b. ~~They are issued by institutions which have long term debt rated "A" or higher by S&P or "A2" or higher by Moody's; and/or have short term debt rated at least A1 by S&P or P1 by Moody's; and~~
- b. The maturity of such deposits does not exceed 365 days.

6. ~~Negotiable Certificates of Deposit (NCDs) issued by a nationally or state-chartered bank, a savings association or a federal association (as defined by Section 5102 of the Financial Code), or by a federally or state-licensed branch of a foreign bank, provided that: **Negotiable certificates of deposit (NCDs)**, provided that:~~

- a. ~~Investments made in accordance with this section plus deposits made under section III (7) of this policy may not exceed 30% of the total portfolio;~~
- b. ~~They are issued by institutions which have long-term obligations which are rated "A" or higher by a nationally recognized statistical rating organization; and/or have short-term debt obligations rated "A" or higher, or the equivalent by a nationally recognized statistical rating organization; They are issued by institutions which have long term debt rated "A" or higher by S&P and Moody's; and/or have short term debt rated at least A1 by S&P or P1 by Moody's;~~
- c. The maturity does not exceed ~~180 days~~5 years; and
- d. No more than ~~30~~5% of the total portfolio may be invested in ~~NCDs~~per issuer.

7. ~~Certificates of Deposit Placement Service (e.g CDARS or like services) using private sector entity to assist in the placement of deposits above federal insurance amounts in increments less than federal insurance at participating banks, savings and loans, or credit unions nationally through a "selected depository institution" in California, provided that:~~

- a. ~~Such deposits plus negotiable certificates of deposit purchased pursuant to Section III (6) of this policy do not exceed 30% of the City's funds available for investment;~~
- a.b. ~~The full amount of the principal and the interest that may be accrued during the maximum term of each certificate shall at all times be insured by the FDIC or the NCUA;~~

- c. The selected depository institution shall be a nationally or state-chartered bank, savings and loan, or credit union in California and shall serve as the custodian for each certificate of deposit issued by the placement service for the City's account;
- d. At the same time the City's funds are deposited and the certificates of deposit are issued, the selected depository institution shall receive an amount of deposits from other commercial banks, savings banks, savings and loan associations or credit unions that, in total, are equal to or greater than the full amount of the principal that the City initially deposited with the selected depository institution;
- e. No credit union may act as a selected depository institution unless:
  - 1. The credit union offers federal depository insurance through the NCUA; and
  - 2. The credit union is authorized by the NCUA in the deposit placement services, and affirms that moneys held by those credit unions while participating in a deposit placement service will at all times be insured by a federal government entity.

7.8. **Repurchase agreements** collateralized with securities authorized under Sections III(A1-2) of this policy maintained at a level of at least 102% of the market value of the repurchase agreements, provided that:

- a. The maximum maturity of repurchase agreements shall be 15 days;
- b. No more than 10% of the portfolio shall be invested in repurchase agreements;
- c. Securities used as collateral for repurchase agreements shall be delivered to the City's custodian bank, except that securities used as collateral for the one to seven day repurchase agreements with the City's depository bank may be held in safekeeping by an independent third party bank trustee~~the depository bank's trust department~~ in the name of the City, as evidenced by appropriate receipts of trust; and
- d. The repurchase agreements are the subject of a master repurchase agreement between the City and the provider of the repurchase agreement. The master repurchase agreement shall be substantially in the form developed by the Public Securities Association.

8.9. **Commercial paper**, provided that:

- a. No more than 15% of the portfolio is invested in commercial paper;

- b. The maturity does not exceed 270 days ~~180 days~~ from the date of purchase; and
- a-c. No more than 15% of the portfolio is invested in commercial paper; and
- c. The paper is of "prime" quality of the highest ranking or of the highest letter and number rating as provided for by a nationally recognized statistical-rating organization (NRSRO). The entity that issues the commercial paper shall meet all of the following conditions in either paragraph (1) or paragraph (2):
- (1) ~~(A)~~ Is organized and operating in the United States as a general corporation. ~~(B)~~ Has total assets in excess of five hundred million dollars (\$500,000,000). ~~(C)~~ Has debt other than commercial paper, if any, that is rated "A" or higher by a nationally recognized statistical-rating organization (NRSRO).
- (2) ~~(A)~~ Is organized within the United States as a special purpose corporation, trust, or limited liability company. ~~(B)~~ Has program wide credit enhancements including, but not limited to, overcollateralization, letters of credit, or surety bond. ~~(C)~~ Has commercial paper that is rated "A-1" or higher, or the equivalent, by a nationally recognized statistical-rating organization (NRSRO).

b-d. No more than 5% of the total portfolio may be invested per issuer.

9-10. **State of California Local Agency Investment Fund (LAIF)**, provided that:

- a. No more than 20% of the City's funds may be invested in LAIF;
- b. It is recognized that LAIF has authority to invest in some instruments that are not permitted for Cities under the California Government Code; and
- c. A thorough investigation of the pool/fund is required prior to investing and on a continual basis. City staff will annually perform due diligence analysis of LAIF based on a standardized questionnaire developed to address investment policy and practices.

10-11. **Corporate medium-term notes**, provided that:

- a. Holdings of medium-term notes may not exceed 30% of the portfolio
- a-b. Such notes have a maximum maturity of ~~five~~ 5 years;
- b-c. Such notes are 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;

~~e.d.~~ Such notes are rated ~~in a rating category of "A" or its equivalent or better~~ higher by a nationally recognized statistical rating organization; and ~~Moody's and S&P;~~ and

~~d.e.~~ Holdings of medium-term notes may not exceed 30% of the portfolio. No more than 5% of the total portfolio may be invested per issuer.

~~41-12.~~ **Mortgage pass-through securities and asset-backed securities**, provided that:

~~a.~~ Such securities shall have a maximum stated final maturity of five years;

~~b.~~ Such securities are rated AAA by S&P or Aaa by Moody's; and

a. Purchase of securities authorized by this subdivision may not exceed 20% ~~percent~~ of the portfolio.

b. Such securities shall have a maximum stated final maturity of 5 years;

c. Issued by an issuer having an "A" or higher credit rating for the issuer's debt as provided by a nationally recognized statistical rating organization; and

~~e.d.~~ Such securities are rated in the category of "AAA" by a nationally recognized statistical rating organization.

~~42-13.~~ **Money market mutual funds**, provided that:

a. Holdings of money market funds may not exceed 10% of the portfolio;

~~a.b.~~ Such funds are registered with the Securities and Exchange Commission and are rated AAA by S&P or Aaa by Moody's;

~~b.c.~~ Such funds have retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience investing in the securities and obligations authorized by California Government Code Section 53601 (a through j) and with assets under management in excess of \$500 million;

~~e.d.~~ Such funds include in their prospectus the statement that one of the investment fund's investment objectives is to seek to maintain a net asset value of \$1; and

~~d.e.~~ Such funds invest only in US Treasury and federal agency securities, and in repurchase agreements backed by US Treasury and federal agency securities; and.

~~e. No more than 10% of the City's funds may be invested in money market mutual funds.~~

~~13-14. **Municipal Securities.** These include obligations of the state of California, any other state, and any local Agency within the state of California including the City of Sunnyvale to the extent permitted by federal law, provided that: **Municipal Obligations,** provided that:~~

~~a. Such Municipal Obligations are limited to obligations of the City of Sunnyvale, obligations of any of the states or their agencies, and obligations of any California local agency;~~

~~a. The maturity does not exceed 5 years from the date of purchase;~~

~~b. The rating by a nationally recognized statistical rating organization is in the "A" "A" category or better; and The Municipal Obligations shall have a rating of at least AA by S&P and Aa3 by Moody's; and~~

~~c. For Municipal Obligations in the form of variable rate demand obligations, the obligations shall be supported by a third-party liquidity facility from a financial institution with short-term ratings of at least A-1 by S&P or P-1 by Moody's. The right of the bondholder to tender the obligation converts these obligations to a short term investment.~~

#### 15. Joint Powers Authority (JPA) Pools, provided that

~~a. The JPA is organized pursuant to CGC Section 6509.7;~~

~~b. The Pool invests only in securities and obligations authorized in CGC Section 53601;~~

~~c. The Pool is managed by an investment adviser registered with the SEC or exempt from registration; and~~

~~a-d. Such adviser has not less than five years of experience investing in securities and obligations authorized in CGC Section 53601, and has assets under management in excess of five hundred million dollars (\$500,000,000).~~

#### **B. Prohibited Investment Vehicles and Practices**

1. State law notwithstanding, any investments not specifically described herein are prohibited, including, but not limited to, mutual funds (other than government money market funds as described in Section III A(12), unregulated and/or unrated investment pools or trusts, collateralized mortgage obligations and futures and options.

2. In accordance with Government Code Section 53601.6, investment in inverse floaters, range notes, or mortgage derived interest-only strips is prohibited.
3. Investment in any security that could result in a zero interest accrual if held to maturity is prohibited.
4. Trading securities for the sole purpose of speculating on the future direction of interest rates is prohibited.
5. Purchasing or selling securities on margin is prohibited.
- ~~6. The use of reverse repurchase agreements, securities lending or any other form of borrowing or leverage is prohibited.~~
- ~~7.6. Prohibited investments held in the portfolio at the time of adoption of this policy may be held until maturity at the discretion of the Director of Finance.~~

### **C. Risk/Safety**

The City recognizes that it is subject to the risks of investing in fixed income securities, especially “market risk,” and “call risk” which ~~is the risk~~ are risks that the value of the portfolio will fluctuate with changes in the general level of interest rates, and “credit risk,” which is the risk that a security or a portfolio will lose some or all of its value due to a real or perceived change in the ability of the issuer to repay its debt.

#### ~~1. Mitigating credit risk in the portfolio~~

- ~~a. The diversification requirements included in the Authorized Investments section are designed to mitigate credit risk in the portfolio;~~

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- ~~b. No more than 5% of the total portfolio may be invested in securities of any single issuer, other than the US Government, its agencies and instrumentalities (limited to 30% per issuer), and LAIF. This section does not preclude the investment of up to 10% of the portfolio in short term repurchase agreements, as defined in Section III (A7) above or money market mutual funds as defined in Section III (A12);~~
- ~~c. The City may elect to sell a security prior to its maturity and record a capital gain or loss in order to improve the quality, liquidity or yield of the portfolio in response to market conditions or the City’s risk preferences; and~~
- ~~d. If a security owned by the City is downgraded by either Moody’s or S&P to a level below the minimum quality required by this Investment Policy, it shall be the City’s policy to sell that security as soon as practicable.~~

## 21. Mitigating market risk in the portfolio

The City recognizes that, over time, longer-term portfolios achieve higher returns. On the other hand, longer-term portfolios have higher volatility of return. The City shall mitigate market risk by providing adequate liquidity for short-term cash needs, and by making longer term investments with funds which are not needed for current cashflow purposes. The City further recognizes that certain types of securities, including variable rate securities, securities with principal paydowns prior to maturity, and securities with embedded options, (callable securities), will affect the market risk profile of the portfolio differently in different interest rate environments. The City, therefore, adopts the following strategies to control and mitigate its exposure to market risk:

- a. The City shall maintain a percentage of the portfolio minimum of three months of budgeted operating expenditures in short term securities to provide for cash flows investments; and
- b. The average maturity of the portfolio shall be no greater than 2.5 years.

## 2. Mitigating credit risk in the portfolio

- a. The diversification requirements included in the Authorized Investments section are designed to mitigate credit risk in the portfolio.
- e.b. No more than 5% of the total portfolio may be invested in securities of any single issuer, other than the US Government, its agencies and instrumentalities (limited to 30% per issuer), and LAIF. This section does not preclude the investment of up to 10% of the portfolio in short-term repurchase agreements, as defined in Section III(A8) above, money market mutual funds as defined in Section III(A13), or JPA Pools as defined in Section III(A15).
- c. The City may elect to sell a security prior to its maturity and record a capital gain or loss in order to improve the quality, liquidity or yield of the portfolio in response to market conditions or the City's risk preferences; and
- d. If a security owned by the City is downgraded by either Moody's or S&P to a level below the minimum quality required by this Investment Policy, it shall be the City's policy to sell that security as soon as practicable.

## D. Liquidity

1. A schedule of major revenues and expenditures for a rolling 12-month period shall be maintained and coordinated with investments from a cash flow standpoint to the extent feasible.

2. Investment maturities ~~shall~~may be timed to provide funds for scheduled expenditures not met by anticipated major revenue receipts.
3. To the extent possible, the Ten Year Resource Allocation Plan shall be used for the cash flow projection purposes, and shall be taken into account in determining long term investment strategy.

#### **E. Return Objectives**

1. **Overall objective.** The investment portfolio shall be designed with the overall objective, in order of priority, of safety, liquidity, and return on investment.
2. **Specific objective.** The investment performance objective for the portfolio shall be to earn a market average yield for the reporting period comparable to the yield of a Treasury Security with a similar average life.

### **IV. RESPONSIBILITY AND REPORTING**

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#### **A. Delegation of Authority**

The City Manager is responsible for directing and supervising the Director of Finance and is also responsible to keep the City Council fully advised as to the financial condition of the City.

The Director of Finance is responsible, by Council delegation, for the custody and investment of City funds and the development of procedures to implement this Investment Policy. This delegation requires that the Director of Finance submit a monthly transaction report to the Council accounting for the investment of funds. The Director of Finance is further responsible for the duties and powers imposed on City Treasurers by the laws of the State of California.

The ~~Finance-Treasury~~ Manager (~~Treasury~~) in Finance is responsible for monitoring investment market information, recommending investment strategy for portfolio diversity and timing of maturities, as well as ensuring compliance with the City's Investment Policy. The Investment staff shall maintain current knowledge of technical and legal requirements regarding municipal investments through continued education and maintain active membership in the California Municipal Treasurers Association (CMTA).

The City may employ an investment adviser to invest all or a portion of the City's cash. Such Adviser shall be granted discretion to invest and reinvest the portfolio in accordance with this Investment Policy and must be registered under the Investment Advisers Act of 1940. Selection of broker/dealers used by an external investment adviser retained by the City will be at the sole discretion of the investment adviser.

#### **B. Reporting, Disclosure and Program Evaluation**

The Director of Finance, as Chief Financial Officer and City Treasurer, ~~shall is required to~~ file a quarterly investment report with the City Council and the City Manager within 30 days following the end of the quarter covered by the report. The report shall include the following information:

1. An asset listing showing par value, cost and accurate and complete market value of each security, type of investment, issuer, and interest rate;
2. The Director of Finance shall provide a monthly transaction report to the City Council;
- ~~2.3.~~ A statement of compliance with the Investment Policy; and
- ~~3.4.~~ A statement that the City has adequate funds to meet its cash flow requirements for the next six months.

### **C. Annual Reports**

1. The investment policy shall be reviewed and adopted 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.
2. A report of portfolio performance for the immediately preceding fiscal year shall be presented as part of the annual investment policy review. This report shall include comparisons of the City's performance compared to the return objectives, and shall include a section on compliance with the investment policy.

## **V. INTERNAL CONTROL**

The Director of Finance has established a system of internal controls to ensure compliance with the Investment Policies of the City and ~~Redevelopment Agency of Sunnyvale and~~ the California Government Code. The internal control procedures include segregation of duties in the different phases of an investment transaction, monthly reconciliation of the investment report to the general ledger, and annual policy compliance review by the City's outside auditor. An independent audit is conducted by the City's outside auditors which includes a compliance review of the City's investment activities to the City's Investment Policy, the California Government Code, and Government Accounting Standards Board (GASB) requirements regarding investment disclosures.

**VI. INVESTMENT COMMITTEE OVERSIGHT**

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The Investment Committee consisting of the City Manager, the Assistant City Manager, and the Director of Finance with staff support, may meet as needed to evaluate the portfolio performance and establish current investment strategies in accordance with the adopted Policy and its objectives.

**VII. HISTORY OF COUNCIL ACTIONS**

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Report to Council No.                    85-388

Approved by the City Council on July 30, 1985

Amended by City Council on July 22, 1986

Amended by City Council on August 11, 1987

Amended by City Council on July 18, 1989

Amended by City Council on July 17, 1990

Amended by City Council on July 23, 1991

Amended by City Council on July 28, 1992

Amended by City Council on July 27, 1993

Amended by City Council on August 9, 1994

Amended by City Council on July 25, 1995

Amended by City Council on July 23, 1996

Amended by City Council on July 29, 1997

Amended by City Council on August 4, 1998

Amended by City Council on August 17, 1999

Amended by City Council on September 12, 2000

Amended by City Council on July 31, 2001

Amended by City Council on July 23, 2002

Amended by City Council on August 12, 2003

Amended by City Council on August 17, 2004

Amended by City Council on August 16, 2005

Amended by City Council on August 22, 2006

Amended by City Council on August 21, 2007

Amended by City Council on August 26, 2008

Amended by City Council on October 14, 2008

Amended by City Council on August 11, 2009

Amended by City Council on August 31, 2010

Amended by City Council on August 23, 2011

Amended by City Council on September 11, 2012

City Clerk Certification \_\_\_\_\_

## VIII. GLOSSARY OF INVESTMENT TERMS

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**Agencies.** Shorthand market terminology for any obligation issued by a *government-sponsored entity (GSE)*, or a *federally related institution*. Most obligations of GSEs are not guaranteed by the full faith and credit of the US government. Examples are:

**FFCB.** The Federal Farm Credit Bank System provides credit and liquidity in the agricultural industry. FFCB issues discount notes and bonds.

**FHLB.** The Federal Home Loan Bank provides credit and liquidity in the housing market. FHLB issues discount notes and bonds.

**FHLMC.** Like FHLB, the Federal Home Loan Mortgage Corporation provides credit and liquidity in the housing market. FHLMC, also called “FreddieMac” issues discount notes, bonds and mortgage pass-through securities.

**FNMA.** Like FHLB and FreddieMac, the Federal National Mortgage Association was established to provide credit and liquidity in the housing market. FNMA, also known as “FannieMae,” issues discount notes, bonds and mortgage pass-through securities.

**GNMA.** The Government National Mortgage Association, known as “GinnieMae,” issues mortgage pass-through securities, which are guaranteed by the full faith and credit of the US Government.

**PEFCO.** The Private Export Funding Corporation assists exporters. Obligations of PEFCO are not guaranteed by the full faith and credit of the US government.

**TVA.** The Tennessee Valley Authority provides flood control and power and promotes development in portions of the Tennessee, Ohio, and Mississippi River valleys. TVA currently issues discount notes and bonds.

**Asked.** The price at which a seller offers to sell a security.

**Average Life.** In mortgage-related investments, including CMOs, the average time to expected receipt of principal payments, weighted by the amount of principal expected.

**Banker’s Acceptance.** A money market instrument created to facilitate international trade transactions. It is highly liquid and safe because the risk of the trade transaction is transferred to the bank which “accepts” the obligation to pay the investor.

**Benchmark.** A comparison security or portfolio. A performance benchmark is a partial market index, which reflects the mix of securities allowed under a specific investment policy.

**Bid.** The price at which a buyer offers to buy a security.

**Broker.** A broker brings buyers and sellers together for a transaction for which the broker receives a commission. A broker does not sell securities from his own position.

**Callable.** A callable security gives the issuer the option to call it from the investor prior to its maturity. The main cause of a call is a decline in interest rates. If interest rates decline since an issuer issues securities, it will likely call its current securities and reissue them at a lower rate of interest. Callable securities have reinvestment risk as the investor may receive its principal back when interest rates are lower than when the investment was initially made.

**Certificate of Deposit (CD).** A time deposit with a specific maturity evidenced by a certificate. Large denomination CDs may be marketable.

**Collateral.** Securities or cash pledged by a borrower to secure repayment of a loan or repurchase agreement. Also, securities pledged by a financial institution to secure deposits of public monies.

**Collateralized Mortgage Obligations (CMO).** Classes of bonds that redistribute the cash flows of mortgage securities (and whole loans) to create securities that have different levels of prepayment risk, as compared to the underlying mortgage securities.

**Commercial Paper.** The short-term unsecured debt of corporations.

**Cost Yield.** The annual income from an investment divided by the purchase cost. Because it does not give effect to premiums and discounts which may have been included in the purchase cost, it is an incomplete measure of return.

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

**Credit Risk.** The risk that principal and/or interest on an investment will not be paid in a timely manner due to changes in the condition of the issuer.

**Current Yield.** The annual income from an investment divided by the current market value. Since the mathematical calculation relies on the current market value rather than the investor's cost, current yield is unrelated to the actual return the investor will earn if the security is held to maturity.

**Dealer.** A dealer acts as a principal in security transactions, selling securities from and buying securities for his own position.

**Debenture.** A bond secured only by the general credit of the issuer.

**Delivery vs. Payment (DVP).** A securities industry procedure whereby payment for a security must be made at the time the security is delivered to the purchaser's agent.

**Derivative.** Any security that has principal and/or interest payments which are subject to uncertainty (but not for reasons of default or credit risk) as to timing and/or amount, or any security which represents a component of another security which has been separated from other components ("Stripped" coupons and principal). A derivative is also defined as a financial instrument the value of which is totally or partially derived from the value of another instrument, interest rate, or index.

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

**Diversification.** Dividing investment funds among a variety of investments to avoid excessive exposure to any one source of risk.

**Duration.** The weighted average time to maturity of a bond where the weights are the present values of the future cash flows. Duration measures the price sensitivity of a bond to changes in interest rates. (See modified duration).

**Federal Funds Rate.** The rate of interest charged by banks for short-term loans to other banks. The Federal Reserve Bank through open-market operations establishes it.

**Federal Open Market Committee:** A committee of the Federal Reserve Board that establishes monetary policy and executes it through temporary and permanent changes to the supply of bank reserves.

**Haircut:** The margin or difference between the actual market value of a security and the value assessed by the lending side of a transaction (i.e. a repo).

**Leverage.** Borrowing funds in order to invest in securities that have the potential to pay earnings at a rate higher than the cost of borrowing.

**Liquidity:** The speed and ease with which an asset can be converted to cash.

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

**Margin:** The difference between the market value of a security and the loan a broker makes using that security as collateral.

**Market Risk.** The risk that the value of securities will fluctuate with changes in overall market conditions or interest rates.

**Market Value.** The price at which a security can be traded.

**Marking to Market.** The process of posting current market values for securities in a portfolio.

**Maturity.** The final date upon which the principal of a security becomes due and payable.

**Medium Term Notes.** Unsecured, investment-grade senior debt securities of major corporations which are sold in relatively small amounts on either a continuous or an intermittent basis. MTNs are highly flexible debt instruments that can be structured to respond to market opportunities or to investor preferences.

**Modified Duration.** The percent change in price for a 100 basis point change in yields. Modified duration is the best single measure of a portfolio's or security's exposure to market risk.

**Money Market.** The market in which short-term debt instruments (Tbills, discount notes, commercial paper, and banker's acceptances) are issued and traded.

**Mortgage Pass-Through Securities.** A securitized participation in the interest and principal cash flows from a specified pool of mortgages. Principal and interest payments made on the mortgages are passed through to the holder of the security.

**Mutual Fund.** An entity which pools the funds of investors and invests those funds in a set of securities which is specifically defined in the fund's prospectus. Mutual funds can be invested in various types of domestic and/or international stocks, bonds, and money market instruments, as set forth in the individual fund's prospectus. For most large, institutional investors, the costs associated with investing in mutual funds are higher than the investor can obtain through an individually managed portfolio.

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

**Prepayment Speed.** A measure of how quickly principal is repaid to investors in mortgage securities.

**Prepayment Window.** The time period over which principal repayments will be received on mortgage securities at a specified prepayment speed.

**Primary Dealer.** A financial institution (1) that is a trading counterparty with the Federal Reserve in its execution of market operations to carry out U.S. monetary policy, and (2) that participates for statistical reporting purposes in compiling data on activity in the U.S. Government securities market.

**Prudent Person (Prudent Investor) Rule.** A standard of responsibility which applies to fiduciaries. In California, the rule is stated as "Investments shall be managed with the care, skill, prudence and diligence, under the circumstances then prevailing, that a prudent person, acting in a like

capacity and familiarity with such matters, would use in the conduct of an enterprise of like character and with like aims to accomplish similar purposes.”

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

**Regional Dealer.** A financial intermediary that buys and sells securities for the benefit of its customers without maintaining substantial inventories of securities and that is not a primary dealer.

**Repurchase Agreement (RP, Repo).** Short-term purchases of securities with a simultaneous agreement to sell the securities back at a higher price. From the seller’s point of view, the same transaction is a reverse repurchase agreement.

**Safekeeping.** A service to bank customers whereby securities are held by the bank in the customer’s name.

**Structured Note.** A complex, fixed income instrument, which pays interest, based on a formula tied to other interest rates, commodities or indices. Examples include inverse floating rate notes which have coupons that increase when other interest rates are falling, and which fall when other interest rates are rising, and "dual index floaters," which pay interest based on the relationship between two other interest rates - for example, the yield on the ten-year Treasury note minus the Libor rate. Issuers of such notes lock in a reduced cost of borrowing by purchasing interest rate swap agreements.

**Total Rate of Return.** A measure of a portfolio’s performance over time. It is the internal rate of return, which equates the beginning value of the portfolio with the ending value; it includes interest earnings, realized and unrealized gains, and losses in the portfolio.

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

**Treasury Bills.** All securities issued with initial maturities of one year or less are issued as discounted instruments, and are called Treasury bills. The Treasury currently issues three- and six-month Tbills at regular weekly auctions. It also issues “cash management” bills as needed to smooth out cash flows.

**Treasury Notes.** All securities issued with initial maturities of two to ten years are called Treasury notes, and pay interest semi-annually.

**Treasury Bonds.** All securities issued with initial maturities greater than ten years are called Treasury bonds. Like Treasury notes, they pay interest semi-annually.

**Volatility.** The rate at which security prices change with changes in general economic conditions or the general level of interest rates.

**Yield to Maturity.** The annualized internal rate of return on an investment which equates the expected cash flows from the investment to its cost.