

AGENDA DESCRIPTION:

Consideration and possible action regarding a recommendation by the Investment Advisory Committee to adopt the City's Investment Policy (Fiscal Impact: None)

RECOMMENDED COUNCIL ACTION:

- 1) Adopt City's Investment Policy as submitted; (2) Alternatively, discuss and take other action related to this item.

ATTACHED SUPPORTING DOCUMENTS:

Draft copy of the City of El Segundo Investment Policy with attachments.

FISCAL IMPACT: Included in Adopted Budget

Amount Budgeted: \$None

Additional Appropriation: N/A

Account Number(s): None

ORIGINATED BY: Ralph E. Lanphere, City Treasurer *REL*

REVIEWED BY: Deborah Cullen, Director of Finance *DC*

APPROVED BY: Doug Willmore, City Manager

BACKGROUND AND DISCUSSION:

Section 53646(a) of the California Government Code requires that the investment policy of a local agency be adopted annually by its legislative body. On June 21, 2011, the City's Investment Advisory Committee met and reviewed the attached policy for coming year. The Committee voted unanimously to recommend the attached policy to the City Council for review and approval. It should be noted that the Committee is recommending no changes to the current policy.

November 2, 2011

STATE OF CALIFORNIA }
COUNTY OF LOS ANGELES }
CITY OF EL SEGUNDO } SS

I, Cathy Domann, Deputy City Clerk of the City of El Segundo, California, and ex-officio Clerk of the City Council of said City, do hereby certify and attest the following to be a full and correct action of the City Council at their meeting of August 2, 2011.

- D. REPORTS OF COMMITTEES, COMMISSIONS AND BOARDS

- 5. Consideration and possible action regarding a recommendation by the Investment Advisory Committee to adopt the City's Investment Policy (Fiscal Impact: None)

Ralph Lanphere, City Treasurer, gave a report.

MOTION by Council Member Brann, SECONDED by Mayor Pro Tem Fisher to adopt City's Investment Policy as submitted. MOTION PASSED BY UNANIMOUS VOICE VOTE. 5/0



Cathy Domann, Deputy City Clerk

City of El Segundo Investment Policy

1.0 Policy:

It is the policy of the City of El Segundo to invest public funds in a prudent manner with the primary objectives of, in priority order, safety, liquidity and yield, and in conformance with all state and local statutes governing the investment of public funds.

2.0 Scope:

This investment policy applies to all funds invested on behalf of the City of El Segundo. These funds are accounted for in the City of El Segundo's Comprehensive Annual Financial Report and include:

2.1 Funds:

2.1.1 General Fund

2.1.2 Special Revenue Funds

2.1.3 Capital Project Funds

2.1.4 Enterprise Funds

2.1.5 Trust and Agency Funds

2.1.6 Debt Service Fund

3.0 Prudence:

When investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing public funds, the City Council, Treasurer and other persons authorized to make investment decisions on behalf of the City, shall act with the care, skill, prudence, and diligence under the circumstances then prevailing, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the City.

3.1 The standard of prudence to be used by investment officers shall be the "prudent investor" standard and shall be applied in the context of managing an overall portfolio of money and investments that belong to the public. Investment officers acting in accordance with written procedures and the investment policy and exercising due diligence shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments.

4.0 Objective:

The primary objectives, in priority order, of the City of El Segundo's investment activities shall be:

- 4.1 **Safety:** Safety of principal is the foremost objective of the investment program. Investments of the City of El Segundo shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. To attain this objective, the City shall only invest in high quality securities and it shall diversify its investments in order that potential losses on individual securities do not exceed the income generated from the remainder of the portfolio so as not to harm the City's cash flow and principal. The City shall also structure its portfolio so as to prevent the need to sell securities prior to maturity and it shall not take short positions, that is, selling securities that the City does not own.
- 4.2 **Liquidity:** The City of El Segundo's investment portfolio will remain sufficiently liquid to enable the City of El Segundo to meet all operating requirements which might be reasonably anticipated.
- 4.3 **Returns on investment:** The City of El Segundo's investment portfolio shall be designed with the objective of attaining a return throughout budgetary and economic cycles, taking into account the City of El Segundo's investment risk constraints and the cash flow characteristics of the portfolio.

5.0 Delegation of Authority:

Authority to manage the City of El Segundo's investment program is derived from the following: State of California Government Code Section 53600 et seq. Management responsibility for the investment program is therefore delegated to the City Treasurer, who shall establish written procedures for the operation of the investment program consistent with this investment policy. Procedures should include reference to: safekeeping, wire transfer agreements, collateral/depository agreements and banking service contracts. Such procedures shall include explicit delegation of authority to persons responsible for investment transactions. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the City Treasurer. The City Treasurer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

6.0 Authorized Financial Dealers and Institutions:

The City Treasurer shall transact business only with banks, savings and loans, state and federal credit unions, and securities dealers. The Treasurer shall select and maintain a current list of broker/dealers, as defined by Corporations Code Section 25004, authorized to provide the City investment services. This list of broker/dealers shall be included in the Treasurer's monthly investment report to the City Council. The broker/dealers shall meet the requirements of Government Code Section 53635.5 and Securities & Exchange

Commission Rule 240.15c3-1 (uniform net capital rule). The Treasurer shall keep on file with the City an audited financial statement for each authorized broker/dealer's last complete fiscal year. Each authorized broker/dealer shall execute an acknowledgement that it has read the City's current Investment Policy and that it will abide by the terms and conditions of the Policy. Additionally, each such broker/dealer shall complete the questionnaire attached hereto. City funds shall only be placed in and invested with depositories that meet the requirements of Government Code Sections 53630 et seq.

7.0 Authorized & Suitable Investments:

The City of El Segundo is empowered by California Government Code Section 53600 et seq. to invest in the following types of securities pursuant to the limits imposed by said statute. (A copy of Government Code Sections 53601 and 53601.6 are attached and by reference herein incorporated). Of such permitted investments, City funds may be invested, subject to the maturity and percentage restrictions contained in Government Code Section 53601 and 53601.6, as amended from time to time, as set forth below:

7.1 Permitted Investments/Deposits.

- 7.1.1. Securities of the U.S. Government
- 7.1.2. Certificates of Deposits
- 7.1.3. Negotiable Certificates of Deposit
- 7.1.4. Bankers Acceptances
- 7.1.5. Commercial Paper
- 7.1.6. Local Agency Investment Fund (LAIF)
- 7.1.7. Time deposits
- 7.1.8. Mutual Funds
- 7.1.9. Medium Term Notes
- 7.1.10. County Pooled Funds

8.0 Collateralization:

Collateralization will be required on certificates of deposit pursuant to Government Code Sections 53652 through 53667.

Collateral will always be held by an independent third party with whom the City has a current custodial agreement. A clearly marked evidence of ownership (safekeeping receipt) must be supplied to the City and retained.

9.0 Safekeeping and Custody:

All security transactions entered into by the City of El Segundo shall be conducted on a delivery-versus-payment (DVP) basis pursuant to Government Code Section 53601. Except for certificates of deposit, securities shall be held by a third party custodian designated by the Treasurer and evidenced by safekeeping receipts pursuant to Government Code Section 53608.

10.0 Diversification:

The City of El Segundo will diversify its investment by security type and institution. With the exception of U.S. Treasury securities and authorized pools, no investment shall be made in contravention of Government Code Sections 53601 and 53601.6 or which will cause more than 50% of the entity's total investment portfolio to be invested in a single security type or with a single financial institution.

11.0 Maximum Maturities:

To the extent possible, the City of El Segundo will attempt to match its investments with anticipated cash flow requirements. The City will not directly invest in securities maturing more than five (5) years from the date of purchase pursuant to Government Code Section 53601.

12.0 Internal and External Control:

The Treasurer shall establish internal control procedures such that daily investment activity is being reviewed by the Director of Finance. These procedures shall provide adequate internal controls to insure compliance with this Investment Policy and state law. The procedures shall be reviewed annually by an independent external auditor.

If the City deposits funds in County Treasuries for investment by County Treasurers, the City Treasurer shall review the statements and reports generated pursuant to Government Code Sections 16481.2, 27133, 27134 and 53684 for each County in which the City has deposited funds. Based upon the review process, the Treasurer shall on a quarterly basis provide a written report to the City Council summarizing any failure by the County Treasuries to comply with state law or their own investment policies and any significant investment activity by the County Treasuries.

If any particular investment is downgraded, the Treasurer and Director of Finance will review and determine if a change in that particular investment must be made.

The City Council shall establish a periodic independent external audit of the City's compliance with this Investment Policy.

13.0 Reporting:

The Treasurer shall file a monthly report, which states its relationship to the Statement of Investment Policy. This report must be filed with the City Manager and the City Council and comply with Government Code Sections 53607, 53646 and 53684. The General elements of the monthly reports include, but are not limited to, the following:

- a. Type of investments.
- b. Issues.
- c. Date of maturity.

- d. Par and dollar amount invested
- e. Current market value of securities with maturity in excess of twelve months
- f. Rate of interest.
- g. Statement relating the report to the Statement of Investment Policy

Statement that there are sufficient funds to meet the next 6 month's obligations

County pool investment report

List of current authorized broker/dealers

List of all investments not held by a third party custodian and the reason they are not placed with a third party custodian.

The Treasurer shall provide the California Debt and Investment Advisory Commission (CDIAC) with second and fourth quarter investment portfolio reports in order to comply with Assembly Bill 943 (AB943.) These reports must state the financial assets of the City and contain the information detailed in Government Code section 53646(b). The reports must be filed with the CIDAC within 60 days after the close of the second and fourth quarters of each calendar year.

14.0 Investment Advisory Committee:

The City has established an Investment Advisory Committee (IAC) comprised of the City Treasurer, the Administrative Services Director, an El Segundo Resident (Council appointed) and a member of the investment community (Council appointed). The IAC shall be provided with copies of the monthly reports identified in Section 13. The IAC shall meet the third Tuesday at the end of each quarter to discuss the City's investments and shall communicate in writing any concerns or comments it has with respect to the City's investments or this Investment Policy to the City Council.

15.0 Ethics and Conflicts of Interest:

All participants in the City's investment process shall seek to act responsibly as custodians of the public trust. The City Treasurer, or when appropriate the Deputy City Treasurer, shall avoid any transaction that might impair public confidence in the City's ability to govern and manage the investment of public funds in an effective manner. The City Treasurer, Deputy City Treasurer, or other official charged with the responsibility of making investment decisions shall have no vested interest in any investment being made involving public funds of the City, and shall gain no financial benefit from such investment decisions.

Glossary

Agency. A debt security issued by a federal or federally sponsored agency. Federal agencies are backed by the full faith and credit of the U.S. Government. Federally sponsored agencies (FSAs) are backed by each particular agency with a market perception that there is an implicit government guarantee. An example of federal agency is the Government National Mortgage Association (GNMA). An example of an FSA is the Federal National Mortgage Association (FNMA).

Basis point. A basis point equals one one-hundredth of 1% (.01%).

Book value. The value at which a security is carried on the inventory lists or other financial records of an investor. This value may be the original cost of acquisition of the security, or original cost adjusted by the amortization of a premium or accretion of a discount. The book value may differ significantly from the security's current value in the market.

Broker. A broker brings buyers and sellers together for a commission paid by the initiator of the transaction or by both sides; he does not position or take ownership of the security.

Certificate of Deposit (CD). A deposit of funds, in a bank or savings and loan association, for a specified term that earns interest at a specified rate or rate formula.

Collateralization. Process by which a borrower pledges securities, property or other deposits for the purpose of securing the repayment of a loan and/or security.

Coupon rate. Interest rate, expressed as a percentage of par or face value, that issuer promises to pay over lifetime of debt security.

Current yield (Current Return). A measure of the simple interest annual yield for interest-bearing investments with maturities of one year or more. To calculate the current yield, the annual coupon interest income is divided by the amount paid to acquire the investment. It is important to note that the current yield is only accurate for investments purchased at par. The current yield calculation includes just one income cash flow – the annual interest income. It ignores the profit or loss resulting from discounts and premiums.

Custody. The service of an organization, usually a financial institution, of holding (and reporting) a customer's securities for safekeeping. The financial institution is known as the custodian.

Delivery versus payment (DVP). A settlement procedure where payment for a securities purchase is made simultaneously with the transfer of the purchased securities. The same procedure applies for a securities sale; the securities are transferred as payment is made.

Discount. The difference between the cost price of a security and its value at maturity when quoted at lower than face value. A security selling below original offering price shortly after sale

also is considered to be at a discount.

Discount securities. Securities that do not pay periodic interest. Investors earn the difference between the discount issue price and the full face value paid at maturity. Treasury bills, bankers' acceptances and most commercial paper are issued at a discount.

Diversification. Dividing investment funds among a variety of securities, offering independent returns, to reduce risk inherent in particular securities.

Federal Agency Securities. A variety of securities issued by several Federally sponsored agencies. Some are issued on a discount basis and some are issued with coupons. Several have the full faith and credit guarantee of the U.S. government, although others do not.

Federal Deposit Insurance Corporation (FDIC). A federal agency that insures bank deposits, currently up to \$250,000 per deposit.

Federal funds (Fed Funds). Funds placed in Federal Reserve banks by depository institutions in excess of current reserve requirements. These depository institutions may lend fed funds to each other overnight or on a longer basis. They may also transfer among each other on a same-day basis through the Federal Reserve banking system. Fed funds are considered to be immediately available funds.

Fed Funds Rate. Interest rate charged by one institution lending federal funds to another.

Federal Home Loan Bank (FHLB). The institutions that regulate and lend to savings and loan associations. The Federal Home Loan Banks play a role analogous to that played by the Federal Reserve Banks vis-à-vis member commercial banks.

Federal Home Loan Mortgage Corporation (FHLMC). A U.S. Corporation and instrumentality of the U.S. government. Through its purchases of conventional mortgages, it provides liquidity to the mortgage markets, much like FNMA. FHLMC's securities are highly liquid and widely accepted. FHLMC assumes and guarantees that all security holders will receive timely payment of principal and interest.

Federal National Mortgage Association (FNMA). 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 & Urban Development, H.U.D. 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 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 guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loans associations and other institutions. Security holder is protected by full faith and credit of the U.S. Government. Ginnie Mae securities are backed by FHA, VA or FMHM mortgages. The term pass-through is often used to describe Ginnie Maes.

Liquidity. The quality of an asset that permits it to be converted quickly into cash without a significant loss of value.

Local Agency Investment Fund (LAIF). A special fund in the State Treasury which local agencies may use to deposit funds for investment and for reinvestment. It offers high liquidity can be converted to cash in 24 hours and no interest is lost. All interest is distributed to those agencies participating on a proportionate share determined by the amounts deposited and the length of time they are deposited.

Market Value. The price at which a security is currently being sold in the market.

Maturity Date. The specified day on which the issuer of a debt security is obligated to repay the principal amount, or face value, a security.

Par Value. The stated or face value of a security expressed as a specific dollar amount marked on the face of the security; the amount of money due at maturity. Par value should not be confused with market value.

Primary Dealer. A group of government securities dealers that 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. A standard of conduct where a person acts with care, skill, prudence, and diligence when investing, reinvesting, purchasing, acquiring, exchanging, selling and managing funds. The test of whether the standard is being met is if a prudent person acting in a similar situation would engage in similar conduct to ensure that investments safeguard principal and maintain liquidity.

Rate of Return. The amount of income received from an investment, expressed as a percentage. *A market rate of return* is the yield that an investor can expect to receive in the current interest-rate environment utilizing a buy-and-hold to maturity investment strategy.

Safekeeping. A procedure where a third party acting as custodian for a fee holds securities.

Secondary Market. Markets for the purchase and sale of any previously issued financial instrument. The first sale of a financial instrument by the original issuer is said to be done a primary market. All subsequent trades are said to be secondary market.

Settlement Date. The date on which a trade is cleared by delivery of securities against funds. The date may be the same date as the trade date or later.

Total return. Interest income paid on the invested principal, plus interest income earned from the successive reinvestment of that income, plus projected capital gains (or minus losses) on the investment. Differs from yield to maturity because (1) it can include gains or losses from sales prior to maturity, and (2) it permits the assumption of a reinvestment rate different from the yield earned on the underlying principal.

Trade Date. The date on which a transaction is initiated or entered into by the buyer and seller.

Treasury Bills. Short-term U.S. government non-interest bearing debt securities with maturities of no longer than one year and issued in minimum denominations of \$10,000. Auctions of three- and six-month bills are weekly, while auction of one-year bills are monthly. The yields on these bills are monitored closely in the money markets for signs of interest rate trends.

Treasury Notes. Intermediate U.S. government debt securities with maturities of one to 7 years.

Treasury Bonds. Long-term U.S. government debt securities with maturities of 10 years or longer. Currently, the longest outstanding maturity is 30 years.

Yield. Loosely refers to the annual return on an investment expressed as a percentage on an annual basis. For interest-bearing securities, the yield is a function of the rate, the purchase price, the income that can be earned from the reinvestment of income received prior to maturity, call or sale and the time from purchase to maturity, call or sale. Different formulas or methods are used to calculate yield. See Yield to Maturity and Total Return Analysis.

Yield-to-maturity. The rate of return yielded by a debt security held to maturity when both the interest payments and investor's potential capital gain or loss are included in the calculation of the return.

