

CITY OF
ARROYO GRANDE



INVESTMENT POLICY

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Prepared by the Administrative Services Department

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CITY OF ARROYO GRANDE

STATEMENT OF INVESTMENT POLICY

Investment Policy

The purpose of this document is to identify various policies and procedures that enhance opportunities for a prudent and systematic investment process and to organize and formalize investment-related activities. The ultimate goal is to enhance the economic status of the City of Arroyo Grande while protecting its cash resources.

The investment policies and practices of the City of Arroyo Grande and the Successor Agency to the Dissolved Arroyo Grande Redevelopment Agency are based on state law and prudent money management. All funds will be invested in accordance with the City's Investment Policy and the authority governing investments for municipal governments as set forth in the California Government Code.

Investment Objective

The investment objective of the City of Arroyo Grande is to optimize the following goals:

- Safety
- Liquidity
- Yield

Safety of principal is the foremost objective of the City. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. Investment decisions should not incur unreasonable credit or market risks in order to obtain current investment income. Credit risk is the risk of loss due to the failure of the security issuer or broker. Market risk is the risk that the market value of securities in the portfolio will fall due to changes in general level of interest rates.

The City's investment portfolio will remain sufficiently liquid to enable the City to meet its cash flow requirements. Liquidity of the investments guarantees the City's ability to meet operating expenditures.

The City's investment portfolio shall be designed with the objective of attaining a market rate of return on its' investments consistent with the constraints imposed by its safety objective and cash flow considerations. Yield is to be a consideration only after the basic requirements of safety and liquidity have been met.

Optimization means striving to achieve a balance between all three objective goals. Should a demand be perceived to prioritize the three goals, they are listed in preferred order.

Prudence Standard

The standard of prudence to be used by the Treasurer and/or deputy shall be the “prudent person rule” and shall be applied in the context of managing City investments. Persons acting in accordance with written procedures and exercising due diligence shall be relieved of personal responsibility for an individual investment loss, provided that deviations are reported in a timely fashion, and appropriate action is taken to control adverse developments.

Areas of Investment Policy

Authorities, Control and Care:

1. The City Treasurer may appoint a Deputy with the responsibility for the individual placement of monies in deposit/investment transactions.
2. The Director of Administrative Services has been authorized, via Resolution #4005, to establish deposit and investment agreements and undertake deposit/investment transactions on behalf of the City of Arroyo Grande.
3. The Administrative Services Department is responsible for implementing this policy, and maintaining a system of internal control designed to prevent employee error or imprudent actions, misrepresentation by parties to an investment agreement, fraud, or unexpected changes in the financial market place.
4. State of California Government Code Sections 53600 et seq. 53683 and 16429.1 regulate the deposit/investment activities of general law cities (See Sec. 53635 and 16429.1). Based upon the relatively small size of the City's portfolio, the City does not utilize a professional investment manager. Rather, Arroyo Grande's investment program is simply a part of the City's financial management activity.
5. The Treasurer and/or deputy shall use good judgment and care, as a "prudent person" would, when entering contracts for deposits and investments, and when placing individual investment transactions. Such care is that which would be exercised by a person concerning his/her own affairs; not for speculation, but for safe investment and earned interest.

Some level of risk is present in any investment transaction. Losses could be incurred due to market price changes, technical cash flow complications such as the need to withdraw a non-negotiable Time Certificate of Deposit early, or even the default of an issuer. To minimize such risks, diversification of the investment portfolio by institution and by investment instruments will be used as much as is practical and prudent.

Portfolio Diversification:

1. Eligible Financial Institutions:

Government Code Section 53635 distinguishes between "deposits" and "investments". It provides that "as far as possible" City monies shall be "deposited" in State or National banks, or State or Federal savings and loan associations; or may be "invested" in specified instruments. Thus, eligible financial institutions would include:

A. Banks plus savings and loans, primarily for active demand deposits (checking accounts and passbook savings) and inactive deposits (non-negotiable Time Certificates), also for investment instruments. See Government Code Sec. 53638 for maximum deposit limitations for banks and savings and loans, involving bank paid up capital and saving and loan net worth.

B. Brokers and issuers, for various investment instruments listed below.

2. Code Authorized Instruments and Portfolio Limitations:

A. Instruments and Portfolio Limitations are authorized as provided in Government Code Section 53635 and 16429.1, as follows:

- 1) Bonds issued by the City of Arroyo Grande. No limit.
- 2) U.S. Treasury Notes, bonds, bills, or other certificates of indebtedness. The maximum maturity shall not exceed five years.
- 3) California State registered notes, bonds, or warrants. Maximum maturity of five years.
- 4) Other local agencies within California, bonds, notes, warrants, or other indebtedness. Five year maximum maturity.
- 5) Obligations issued by Federal agencies such as Federal Home Loan Bank (FHLB), Federal Home Loan Mortgage Corporation (FHLMC), Federal Farm Credit Bank (FFCB), etc. Limited to a five year maximum maturity.
- 6) Banker's acceptances (bills of exchange or time drafts) drawn on and accepted by a commercial bank, and which are eligible for purchase by the Federal Reserve System. These are limited to 40 percent of the City's surplus funds, and limited to 180-day maximum maturities.
- 7) Commercial paper of "prime" quality, as rated by Moody's Investor Service or Standard and Poor's Corporation. These are limited to 25 percent of the City's portfolio, and limited to 270-day maximum maturities, plus some other qualifications.

- 8) FDIC insured or fully collateralized time certificates of deposit in financial institutions located in California, including United States branches of foreign banks licensed to do business in California. The maximum maturity of a time deposit shall not exceed five years.
- 9) Negotiable Certificates of Deposit, issued by either a National or State bank or a state or federal savings and loan provided that the senior debt obligations of the issuing institution are rated “AA” or better by Moody’s or Standard & Poor’s. The maximum maturity of a negotiable certificate of deposit shall not exceed five years. Purchase of negotiable certificates of deposit may not exceed 20 percent of the book value of the City’s portfolio.
- 10) Repurchase agreements or reverse repurchase agreements, whereby the seller of securities will repurchase them on a specified date and for a specified amount. The maximum maturity of a time deposit shall not exceed one year.
- 11) Local Agency Investment Fund, State of California, per Government Code Sec. 16429.1. Pooled monies of various agencies within California. Account size is limited to a minimum of \$5,000 (unless bond proceeds) and a maximum limit of \$50 million.

Safekeeping of Securities:

To protect against fraud or embezzlement or losses caused by collapse of an individual securities dealer, all securities owned by the City shall be held in safekeeping by a third party bank trust department. Designated third party shall act as agents for the City under the terms of a custody agreement. All trades executed by a dealer will settle delivery vs. payment (DVP) through the City’s safekeeping agent. Investment officials shall be bonded to protect the public against possible embezzlement or malice.

Securities held in custody for the City shall be independently audited on an annual basis to verify investment holdings.

City Placement Practice:

1. The following financial institutions will be used by the City of Arroyo Grande, for non-negotiable Time Certificates of Deposit:
 - a) Commercial banks having offices in the State of California (preference will be given to local banks if interest rates are the same).
 - b) Savings and loans maintaining offices in the State of California.
2. The State of California Local Agency Investment Fund (L.A.I.F.) will be utilized, to pool current surplus City monies for demand deposit earnings.

3. For other investment instruments, three institutions may be selected from a list of qualified primary or regional broker/dealers qualifying under SEC rule 15c3-1 (uniform net capital rule). Broker/dealers must be licensed in the State of California and be headquartered or maintain a branch office in the State of California.

All brokers/dealers shall carry Errors and Omissions insurance with a limit of not less than \$1,000,000 per occurrence. Proof of existence of said insurance shall be provided to the City at its request and the City shall be notified if the policy is cancelled or coverage is reduced below \$1,000,000.

4. Prior to establishing a contract for deposit of monies per Sec. 53649, or placing an individual investment, the credit-worthiness of each financial institution will be determined. As a minimum, the ratio of net worth (equity) to total assets shall be 3.0% or more.
5. No more than 30% of the City's available surplus shall be placed with any one financial institution (excluding the State L.A.I.F. and government agency issues).
6. No more than 50% of the City's available surplus shall be placed with savings and loan institutions.
7. The City, as authorized in Government Code Sections 53635 and 16429.1, may use all deposit and investment instruments; except repurchase and reverse repurchase agreements shall not be used. However, non-negotiable time certificates with commercial banks and savings and loans, plus deposits in the State Local Agency Investment Fund, will be the primary instruments used by the City, along with possible U.S. Treasury bills and bankers acceptances.
8. Collateral security on Certificates of Deposit will be provided in accordance to Government Code Sections 53651 and 53653 by the commercial banks and savings and loans, at 110% when government securities are used, or at 150% when promissory notes secured by 1st mortgages or 1st trust deeds on improved residential real property located in California are used.
9. Individual placements of deposits and investments will be made based upon highest rate quotes, in most instances.
10. Within the context of any portfolio limitations and quoted rates, deposits shall be distributed between institutions as evenly as practical or possible.

Cash Management and Maturities:

1. A maximum investment of all City monies, not needed to meet current cash flow needs, will be maintained as closely as practical. A sufficient compensating balance will also be provided, regarding the City's banking service agreement.

2. All monetary resources will be pooled for investment purposes, to maximize interest earnings, which will be periodically allocated to the various funds of the City based upon average cash balances at month ends. No interest will be credited to individual accounts within the various funds.
3. Time deposits and investments will be held to maturity, unless it is absolutely necessary to sell an investment early due to an unexpected liability.
4. Maturities of deposits and investments will be scheduled in such a manner as to provide a steady stream of available cash to meet cash flow needs. The California State Local Agency Investment Fund deposits of the City of Arroyo Grande are available on a same-day/next-day telephone call basis.

Investment Reporting, Policy Review and Effective Policy Term

An Investment Policy is no longer required by statute. However, it is highly recommended by both the Association of Public Treasurers of the United States & Canada and the Government Finance Officers Association (GFOA). It is in the best interest of the City to prepare, present and discuss the Investment Policy with the City Council on an annual basis. In addition, a monthly report is submitted to the City Council, providing the following information:

1. Type of investment.
2. Financial institution (bank, savings and loan, broker, etc).
3. Date of maturity.
4. Principal amount.
5. Rate of interest.
6. Current market value for all securities having a maturity of more than 12 months.
7. Relationship of the monthly report to the annual statement of investment policy.

The City's independent certified public accountant shall review and make recommendations, when appropriate, regarding the City of Arroyo Grande's investment policy.