



## Legislation Text

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**File #:** 18-141, **Version:** 1

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**SUBJECT:** Approval of an Update to the City's Investment Policy

### REPORT IN BRIEF

Considers approving an update to the City's Investment Policy.

### RECOMMENDATION

**City Council** - Adopt a motion adopting **Resolution 2018-22**, a Resolution of the City Council of the City of Merced, California, adopting Investment Policy.

### ALTERNATIVES

1. Adopt as recommended by staff; or
2. Refer back to staff with specific direction.

### AUTHORITY

California Government Code Section 53646, subdivision (a)(2)

### CITY COUNCIL PRIORITIES

As provided for in the 2017-18 Adopted Budget

### DISCUSSION

Current investment law states that the Finance Officer may annually render to the legislative body a statement of investment policy, which the legislative body shall consider at a public meeting. Any change in the policy shall be considered by the legislative body at a public meeting.

A good investment policy drives the cash, treasury, and investment management functions of an agency. It serves as a guide for setting and achieving program objectives, defines rules and establishes benchmarks, and reduces the exposures to liability of the investment staff and the governing board.

On March 5, 2018, the City Council approved a Professional Service Agreement with Chandler Asset Management for Investment Advisory Services. The scope of service included the extensive review of the City's investment policy to ensure it appropriately embodies the City's investment objectives, risk profile and expected outcomes as well as applicable laws and industry best practices.

The City of Merced met with Chandler Asset Management to discuss and review all proposed changes to the Investment Policy. The revised modifications encompass changes to the California

Government Code, include the latest California best practices and enhance the clarity and readability of the policy. A brief summary of the changes is below:

### **Scope**

- Inclusion of language specifying that debt service funds included in the scope of this policy refer to monies related to inter-fund borrowing to differentiate from bond-related funds which are subject to bond covenants (and not this policy).

### **Prudence**

- Replacement of the policy's Prudent Person Standard with the Prudent Investor Standard which is the standard required by Code Section 53600.3.

### **Objectives**

- A move of any language discussing possible benchmarks to a separate section addressing investment program performance evaluation. Moreover, addition of language that specifies the City seeks to generate a market rate of return commensurate with the risk parameters of the portfolio.

### **Delegation of Authority**

- Inclusion of language permitting the City to engage the services of a professional investment adviser.
- Inclusion of language requiring the professional management of the portfolio, with measured losses to be considered in the overall context of the portfolio and cash flow requirements of the City. Although investments are structured to provide cash when needed without the need to liquidate funds, periodic losses may be realized temporarily when sales before maturity occur to improve the overall yield of the portfolio.

### **Authorized Financial Dealers and Institutions**

- Updates to this section to include the most current best practices, including:
  - A requirement that all transactions be completed via a competitive process
  - A requirement that the Finance Officer establish procedures for the selection of authorized financial dealers and institutions
  - A description of the types of financial institutions that are permitted to do business with the City
  - A requirement that any financial institution that does business with the City acknowledge reviewing Code Section 53600 et. seq. and the City's investment policy
  - An acknowledgement that the City's investment adviser may maintain its own list of financial dealers and institutions

### **Authorized and Suitable Investments**

- Expansion of the descriptions of authorized investments and added additional requirements for U.S. Treasury obligations, Federal Agency securities, certificates of deposit, Local Agency Investment Fund, passbook savings, bankers' acceptances, commercial paper, medium-term notes, repurchase agreements, Local Agency Investment Fund ("LAIF"), and mutual funds. The requirements bring concentration limits and credit requirements in line with Code, and add

an additional limit of 5% per issuer on certain asset classes.

- Inclusion of asset classes allowable by Code. We believe that inclusion of these additional asset classes will provide the City additional diversification and may enhance long-term returns:
  - Municipal securities from the State of California and its political subdivisions
  - Municipal securities from the treasuries or agencies of the other 49 states
  - Negotiable certificates of deposit
  - Pass-through securities such as asset-backed and mortgage-backed securities, and collateralized mortgage obligations
  - Supranational securities

### **Prohibited Investment Vehicles and Practices**

- Addition of a new section to the policy specifying prohibited investments as specified by Code.
- Inclusion of a prohibition on trading for speculation only and trading on margin.

### **Investment Pools/Mutual Funds**

- Addition of a new section to the policy requiring due diligence in the use of investment pools and mutual funds.

### **Delivery, Safekeeping and Custody**

- Augmentation of language requiring delivery versus payment when trading securities, as well as a requirement that the City's funds shall be held in a third-party custodial safekeeping arrangement.

### **Risk Management and Diversification**

- Inclusion of language requiring steps to mitigate both credit and market risk. The requirements include:
  - A 5% per issuer limit on all security types unless otherwise specified
  - Sales before maturity which are permitted under specified circumstances
  - A policy to handle securities that have been downgraded below the minimum allowable credit quality
  - A requirement to maintain a minimum of six months of operating expenses in short-term investments to provide for expected disbursements
  - A 20% limit on callable securities
  - A maturity limit of five years unless allowed otherwise specified by the policy
  - A portfolio duration limit of 20% +/- the benchmark duration

### **Review of the Investment Portfolio**

- Inclusion of language requiring that the portfolio be reviewed no less than quarterly to ensure all investments comply with the investment policy.

### **Maximum Maturities**

- Inclusion of language requiring any investments longer than five years will require City Council

approval no less than 90 days prior to the first investment.

### **Performance Evaluation**

- Inclusions of language requiring the Finance Officer to adopt a benchmark to measure the progress of the investment program.

### **Glossary**

- Update of the policy's Glossary.

The investment policy was last updated in 2016 when it adopted Resolution No. 2016-11. The only changes at that time were minor updates to language and definitions.

### **IMPACT ON CITY RESOURCES**

No appropriation of funds is needed.

### **ATTACHMENTS**

1. Investment Policy 2016
2. Resolution with Investment Policy 2018-22