

CITY OF REDWOOD CITY
INVESTMENT POLICY

PURPOSE: The purpose of this policy is to provide guidelines for investment of the City's funds.

I. Policy

The City shall invest public funds in such a manner as to comply with all federal, state, and local statutes governing the investment of public funds; ensure prudent money management; provide for daily cash flow requirements; and meet the objectives of the Policy, in priority order of safety, liquidity, and return on investment.

II. Scope

- A. Investments for all the funds in the custody of the City, including funds belonging to other agencies and entities, such as the Port and Successor Agency to the former Redevelopment Agency, for which the City acts as fiscal agent will be made on a pooled basis. These funds are normally accounted for in the City's Comprehensive Annual Financial Report (CAFR), which includes the annual independent audit report, under the following categories:
 - 1. General Fund
 - 2. Special Revenue Funds
 - 3. Capital Project Funds
 - 4. Debt Service Funds
 - 5. Enterprise Funds
 - 6. Internal Service Funds
 - 7. Agency Funds
- B. The City Council may, on the recommendation of the City Manager and the City Treasurer, expressly authorize exceptions to this policy.
- C. If, at the time this policy is adopted, the portfolio holds investments which were made in the past and in accordance with previous policies and existing federal and State laws but do not meet the provisions of this policy, such past investments are grandfathered as permissible investments. The City may choose to hold such investments until maturity; however, their maturity cannot be extended without the express authorization of the City Council.
- D. Funds excluded from this policy:
 - 1. Bond Proceeds – Proceeds of debt issuance shall be invested in accordance with the City's general investment philosophy as set forth in this policy. The overriding policy for the investment of bond proceeds will be dictated by the bond documents governing such funds as long as the documents are approved by the City Council or related governing board.
 - 2. Deferred Compensation, Retirement, Section 115 Trust, and Other Post Employment Benefit Plans – Investments related to these plans are not subject to this policy since third-party administrators or trustees manage the funds and either the individual plan participants or outside investment managers or trustees direct investment selections under the guidelines established by City Council.

CITY OF REDWOOD CITY
INVESTMENT POLICY

III. Investment Philosophy

- A. The City's investment philosophy is based on the Prudent Investor Standard as set forth in California Government Code 53600.3:

"...all governing bodies of local agencies or persons authorized to make investment decisions on behalf of those local agencies investing public funds pursuant to this chapter 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 agency, 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 agency. Within the limitations of this section and considering individual investments as part of an overall strategy, investments may be acquired as authorized by law."

- B. The investment securities are purchased with the intention to hold until maturity. Sale of securities prior to maturity is permitted where it serves the City's investment objectives.

IV. Objectives

- A. The City's investment philosophy sets the tone for the policies, practices, procedures and objectives that control the investment function. The investment of funds will be guided by the primary objectives of safety, liquidity, and a reasonable market rate of return, in this order of priority.

1. Safety – Safety of principal is the foremost objective of the investment program. The City will undertake investments in a manner that ensures the preservation of capital in the portfolio taken as a whole. To ensure the safety of principal, the City will seek to minimize credit risk (defined as the risk of default on the part of the issuer of a security) by diversification and by investing in high quality investments and also to minimize market risk (defined as the risk of fluctuations in the market value of securities) by limiting the weighted average maturity of the investment portfolio to 3 years.
2. Liquidity – The City will maintain sufficient cash and short-term investment instruments which, together with projected revenues, will provide sufficient liquidity to meet all cash flow requirements which might be reasonably anticipated including contingencies for six months.
3. Return on Investment (Yield) – The City's investment portfolio will be designed with the objective to attain a market rate of return throughout economic cycles, commensurate with the City's investment risk constraints and the cash flow characteristics of the portfolio.

- B. The investment function will have the ongoing objectives of assuring compliance with Federal, State and local laws governing the investment of public funds, providing for short term and long term cash flow needs, and establishing appropriate standards and limits for the type of investments made and the issuers of such investments.

CITY OF REDWOOD CITY
INVESTMENT POLICY

V. Delegation of Authority

- A. The City of Redwood City Municipal Code Section 2.33.1 specifies that the City Treasurer (Assistant City Manager of Administrative Services) is authorized to invest or deposit the City's funds in accordance with this policy, California Government Code Sections 53600 and 53630 et seq. and all other related Federal and State laws. In the absence of the City Treasurer, and unless otherwise delegated, the Deputy Treasurer will serve as the acting Treasurer. The City Treasurer may appoint the Deputy Treasurer to act on behalf of the City. The City Treasurer will provide written authorization in delegating any of his/her authority.
- B. The City Manager will provide periodic oversight to the investment function which includes but is not limited to reviewing quarterly investment reports issued by the City Treasurer.
- C. The City Council's primary responsibilities over the investment function include approving the Investment Policy, annually reviewing such policy, reviewing quarterly investment reports issued by the City Treasurer, authorizing bond documents and other unique financing transactions, and authorizing any deviations from the City's investment policies.
- D. The Finance/Audit Sub-Committee of the City Council will act in an advisory capacity and provide oversight to the investment function through the periodic review of the investment report and policy.
- E. The City may engage the services of one or more external investment managers/advisors to assist in the management of the City's investment portfolio in a manner consistent with the City's objectives. Such external managers may be granted discretion to purchase and sell investment securities in accordance with this Investment Policy. Such managers must be registered under the Investment Advisers Act of 1940. The City is currently in contract with PFM Asset Management for Investment Advisory Services through FY 2018-19.

VI. Ethics and Conflict of Interest

- A. All officials, staff members and consultants, involved in the investment functions will refrain from personal business activity that could conflict with the performance of the investment function or which may impair their ability to make impartial investment decisions. All investment personnel shall comply with reporting requirements of applicable State laws including annual filling of a Statement of Economic Interest. The Treasurer and staff shall avoid any transaction that might impair public confidence in the City.
- B. Officials, staff members and consultants shall further disclose any personal financial positions that could be related to the City's cash and investment portfolio.
- C. All bond issue participants, including but not limited to, underwriters, bond counsels, disclosure counsels, financial advisors, brokers and dealers will disclose any fee sharing arrangements or fee splitting to the Treasurer prior to the execution of any transactions. The providers must disclose the percentage and approximate dollar amount of their share to the City prior to the execution of any transactions.

CITY OF REDWOOD CITY
INVESTMENT POLICY

VII. Investment Controls

- A. The City Manager shall oversee and ensure that the City Treasurer implements and maintains a system of internal investment controls and segregated responsibilities of the investment function in order to prevent fraud, theft, loss of principal, loss of control over funds, inaccurate reporting, negligence, and over-reliance on a single employee for investment decisions.
- B. Internal controls should include but are not limited to:
 - 1. Segregation of duties (e.g., the purchaser of investments is different than the person recording the transaction)
 - 2. Reconciliation of investment report and cash balances
 - 3. Authorization of transactions
- C. The external City auditor will review the investment program annually in order to provide reasonable assurance that the policy and procedures are complied with.

VIII. Authorized Financial Dealers and Institutions

- A. The City Treasurer or designee will obtain financial information from qualified institutions to determine if the institution markets in securities appropriate to the City's needs, can assign qualified sales representatives, and can provide written agreement to abide by the conditions set forth in the this Policy.
- B. The City Treasurer will maintain a list of financial institutions and broker/dealers authorized to provide investment services to the City. An eligible designation does not guarantee that the City will do business with the firm or institution.
- C. If the City utilizes an external investment manager/advisor, the manager will perform due diligence and maintain their own list of approved broker/dealers. The manager is authorized to transact with its own approved broker/dealer list on behalf of the City. Such managers must be registered under the Investment Advisers Act of 1940.
- D. The following criteria will be used in determining investment providers:
 - 1. Broker/Dealers: The purchase by the City of any investment other than those purchased directly from the issuer shall be purchased from a broker/dealer firm designated as a Primary Government Dealer by the Federal Reserve Bank of New York or a regional dealer that qualifies under SEC Rule 15C3-1 (uniform net capital rule).
 - 2. Banks: The City shall purchase securities from banks which meet all of the following criteria:
 - a. Nationally or State chartered banks
 - b. Registered as investment securities dealers with the Securities and Exchange Commission
 - c. Independently rated "A" or higher by two nationally recognized statistical rating organizations
 - 3. Investment Bankers, Underwriters and Financial Advisors: The purchase by the City of any investments from these providers in the course of completing a bond transaction must be expressly authorized by the City Council after such a provider discloses their commission, spread or fee in approximate dollar amount. Otherwise, the acquisition of such

CITY OF REDWOOD CITY
INVESTMENT POLICY

investments must be procured from the broker/dealers customarily used by the City.

4. The Federal Reserve Bank: Direct purchases of Treasury bills, notes and bonds from the U.S. Federal Reserve Banks branches are allowed and are exempt from quality requirements of section VIII of this policy.

- E. All financial institutions and broker/dealers who desire to become qualified bidders for investment transactions must provide the following information to the City Treasurer:
 1. A completed City of Redwood Broker/Dealer Questionnaire
 2. Audited financial statements
 3. Proof of Financial Industry Regulatory Authority (FINRA) certification
 4. Proof of state registration
 5. Certification of having read and willingness to comply with City's investment policy.

- F. The City Treasurer will conduct an annual review of the financial condition and registrations of brokers/dealers on the City's approved list.

- G. A current audited financial statement is required to be on file for each financial institution and broker/dealer with which the City invests.

- H. Certificates of deposit will not be placed with an institution once it has received a Cease and Desist order from any bank regulatory agency.

IX. Authorized Investments (with limitation and quality guidelines)

The California Government Code sections 53600 et seq. governs the allowable investments into which a local government agency can enter. These Government Code sections also stipulate as to the portfolio percentage limits and investment quality standards for some but not all permitted investments. The Government Code sections provide a starting point for establishing the City quality standards, percentage limits and maturity levels. Should the Government Code become more restrictive than this policy, the Government Code restrictions shall prevail.

Whenever a maximum allowable percentage of the portfolio is stipulated for any type of security as detailed below, the limit or maximum allowable is determined by the portfolio size or composition at the close of the date on which the security is purchased.

Additional requirements related to some investment types are detailed in the following sections of this policy.

A. United States Treasury Obligations – No Maximum

United States Treasury bills, notes, bonds, or those for which the full faith and credit of the United States are pledged for payment of principal and interest. There is no limitation on the percentage of the portfolio that can be invested in this category, although a five-year maturity limitation is applicable.

B. Federal Agency or Government Sponsored Enterprises (GSEs) – No Maximum

CITY OF REDWOOD CITY
INVESTMENT POLICY

Federal agency or United States government-sponsored enterprise obligations, participations, or other instruments, including those issued by or fully guaranteed as to principal and interest by federal agencies or United States government-sponsored enterprises.

C. LOCAL AGENCY INVESTMENT FUND (LAIF) – Maximum \$65M per account (current State rules)

The City may invest in the LAIF established by the State Treasurer for the benefit of local agencies up to the maximum permitted under its rules. The aggregate investment in such securities shall not exceed \$65 million per account.

D. SAN MATEO COUNTY POOL – Maximum \$50M

The City may invest in the San Mateo County Pool established by the San Mateo County Treasurer for the benefit of local agencies (as established in California Code Section 53684). The aggregate investment in such securities shall not exceed \$50 million.

E. State and Local Agency Bonds – Maximum 20%

Registered state warrants or treasury notes or bonds of this state, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the state or by a department, board, agency, or authority of the state.

Registered treasury notes or bonds of any of the other 49 states in addition to California, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of any of the other 49 states, in addition to California.

Bonds, notes, warrants, or other evidences of indebtedness of a local agency within this state, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the City, or by a department, board, agency, or authority of the City.

Securities eligible for investment under this section must be rated in a rating category of “A” or its equivalent or better by a NRSRO. No more than 5% of the portfolio may be invested in a single issuer. The aggregate investment in such securities shall not exceed 20% of the City’s total portfolio.

F. Money Market and Mutual Funds – Maximum 20%

(1) Shares of beneficial interest issued by diversified management companies that invest in the securities and obligations as authorized by California Government Code section 53601 subdivisions (a) to (k), inclusive, and subdivisions (m) to (q), inclusive, and that comply with the investment restrictions of this article and Article 2 (commencing with Section 53630). If investment is in shares issued pursuant to this paragraph, the company shall have met either of the following criteria:

(A) Attained the highest ranking or the highest letter and numerical rating provided by not less than two NRSROs.

(B) 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 subdivisions (a) to (k), inclusive, and subdivisions (m) to (q), inclusive, and with assets under management in excess of five hundred million dollars (\$500,000,000).

CITY OF REDWOOD CITY
INVESTMENT POLICY

(2) Shares of beneficial interest issued by diversified management companies that are money market funds registered with the Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. Sec. 80a-1 et seq.). If investment is in shares issued pursuant to this paragraph, the company shall have met either of the following criteria:

(A) Attained the highest ranking or the highest letter and numerical rating provided by not less than two NRSROs.

(B) Retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience managing money market mutual funds with assets under management in excess of five hundred million dollars (\$500,000,000).

The purchase price of shares of beneficial interest purchased pursuant to this subdivision shall not include commission that the companies may charge and shall not exceed 20% of the City's moneys that may be invested pursuant to this section. However, no more than 5% of the City's funds may be invested in shares of beneficial interest of any one mutual fund pursuant to paragraph (1).

In addition, the City may invest in money market and mutual funds that are registered under the Investment Company Act of 1940 that (1) are "no-load" (no commission or fee shall be charged on purchases or sales of shares) and (2) have a constant daily net asset value per share of \$1.00;

G. Local Government Investment Pools – Maximum 20%

Shares of beneficial interest issued by a joint powers authority organized pursuant to Section 6509.7 that invests in the securities and obligations authorized in California Government Code section 53601 subdivisions (a) to (q), inclusive. Each share shall represent an equal proportional interest in the underlying pool of securities owned by the joint powers authority. To be eligible under this section, the joint powers authority issuing the shares shall have retained an investment adviser that meets all of the following criteria:

(1) The adviser is registered or exempt from registration with the Securities and Exchange Commission.

(2) The adviser has not less than five years of experience investing in the securities and obligations authorized in California Government Code section 53601 subdivisions (a) to (q), inclusive.

(3) The adviser has assets under management in excess of five hundred million dollars (\$500,000,000).

H. Medium-Term Corporate Notes– Maximum of 30%

The City may invest in medium term notes, defined as all corporate and depository institution debt securities with a maximum maturity of 5 years or less, 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. Notes eligible for investment under this subdivision shall be rated in a rating category of "A" or the equivalent or better, by an NRSRO. No more than 5% of the City's portfolio may be invested in the medium-term notes of any one issuer or its affiliates. The aggregate investment in such securities shall not exceed 30% of the City's total portfolio.

CITY OF REDWOOD CITY
INVESTMENT POLICY

I. Non-negotiable Certificates of Deposit – Maximum of 10%

The City may invest in non-negotiable certificates of deposit with a maturity not exceeding three years, in state or nationally chartered banks or savings banks that are insured by the FDIC, subject to the limitations of California Government Code Section 53638. Amounts in excess of FDIC insurance coverage shall be secured in accordance with California Government Code Section 53652. The City may use CD Placement Service for ease of administration to benefit from FDIC insured deposits without dealing with many banks. No more than 2% of the City's portfolio may be invested in any one institution. The aggregate investment in such securities shall not exceed 10% of the City's total portfolio.

J. Negotiable Certificates of Deposit – Maximum of 30%

Negotiable certificates of deposit issued by a nationally or state-chartered bank, a savings association or a federal association (as defined by Section 5102 of the Financial Code), a state or federal credit union, or by a federally licensed or state-licensed branch of a foreign bank. For purposes of this section, negotiable certificates of deposit do not come within Article 2 (commencing with Section 53630), except that the amount so invested shall be subject to the limitations of Section 53638. The legislative body of the City and the treasurer or other official of the City having legal custody of the moneys are prohibited from investing City funds, or funds in the custody of the City, in negotiable certificates of deposit issued by a state or federal credit union if a member of the legislative body of the City, or a person with investment decision making authority in the administrative office manager's office, budget office, auditor-controller's office, or treasurer's office of the City also serves on the board of directors, or any committee appointed by the board of directors, or the credit committee or the supervisory committee of the state or federal credit union issuing the negotiable certificates of deposit. Eligible investments under this subdivision shall be rated in a rating category of "A" or its equivalent or better by a NRSRO. No more than 5% of the City's portfolio shall be invested in a single issuer. Purchases of negotiable certificates of deposit shall not exceed 30% of the City's moneys that may be invested pursuant to this section.

K. Prime Commercial Paper – Maximum of 25%

The City may invest in prime commercial paper of the highest ranking or of the highest letter and number rating as provided for by a NRSRO. The entity that issues the commercial paper shall meet all of the following conditions in either sub-paragraph 1 or sub-paragraph 2 below:

1. The entity shall (1) be organized and operating in the United States as a general corporation, (2) have total assets in excess of \$500,000,000 and (3) have debt other than commercial paper, if any, that is rated in a rating category of "A" or its equivalent or better by a NRSRO.
2. The entity shall (1) be organized within the United States as a special purpose corporation, trust, or limited liability company, (2) have program-wide credit enhancements, including, but not limited to, over collateralization, letters of credit or surety bond; and (3) have commercial paper that is rated in a rating category of "A-1" or its equivalent or better by a NRSRO.

Eligible commercial paper shall have a maximum maturity of 270 days or less. The City may invest no more than 25% of their moneys in eligible commercial paper. The City may purchase no more

CITY OF REDWOOD CITY
INVESTMENT POLICY

than 10% of the outstanding commercial paper of any single issuer. No more than 5% of the City's total portfolio shall be invested in the commercial paper of any one issuer.

L. Bankers' Acceptances – Maximum of 10%

The City may invest in Banker's Acceptances otherwise known as bills of exchange or time drafts that are drawn on and accepted by a commercial bank. Purchases of bankers' acceptances shall not exceed 180 days' maturity from the date of trade settlement, be rated at least A-1, or the equivalent, by a NRSRO, drawn on or accepted by a commercial bank with combined capital and surplus of at least \$250 million, whose deposits are insured by the FDIC, and whose senior long-term debt is rated in a rating category of at least "A", or the equivalent, by a NRSRO at the time of purchase. No more than 2% of the City's total portfolio shall be invested in bankers' acceptances of any one issuer, and the aggregate investment in bankers' acceptances shall not exceed 10% of the City's total portfolio.

M. Repurchase Agreements – Maximum 10%

The City may invest in Repurchase Agreements with a final termination date not exceeding 90 days collateralized by U.S. Treasury obligations listed in "A" above and with the maturity of the collateral not exceeding 10 years. For the purpose of this section, the term collateral shall mean purchased securities under the terms of the City's approved Master Repurchase Agreement. The purchased securities shall have a minimum market value including accrued interest of 102% of the dollar value of the funds borrowed. Collateral shall be held in the City's custodian bank, as safekeeping agent, and the market value of the collateral securities shall be marked-to-the-market daily.

Repurchase Agreements shall be entered into only with broker/dealers recognized as a primary dealer by the Federal Reserve Bank of New York, or with financial firms that have a primary dealer within their holding company structure. Approved Repurchase Agreement counterparties shall have a short-term credit rating of at least "A-1", or the equivalent, and a long-term credit rating of at least "A", or the equivalent, by a NRSRO. Repurchase agreement counterparties shall execute a City approved Master Repurchase Agreement with the City. The Finance Director/City Treasurer shall maintain a copy of the City's approved Master Repurchase Agreement along with a list of broker/dealers who have executed same. No more than 2% of the City's total portfolio shall be invested in repurchase agreements with any one counterparty, and the aggregate investment in repurchase agreements shall not exceed 10% of the City's total portfolio.

N. Asset-backed Securities – Maximum 20%

A mortgage passthrough security, collateralized mortgage obligation, mortgage-backed or other pay-through bond, equipment lease-backed certificate, consumer receivable passthrough certificate, or consumer receivable-backed bond. Securities eligible for investment under this subdivision shall be rated in a rating category of "AA" or its equivalent or better by an NRSRO and have a maximum remaining maturity of five years or less. Purchase of securities authorized by this subdivision shall not exceed 20% of the City's surplus moneys that may be invested pursuant to this section. No more than 5% of the City's portfolio shall be invested in a single issuer.

O. Supranational Securities – Maximum 30%

United States dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank, with a maximum remaining maturity of five years or less, and eligible for purchase and sale within the United States.

CITY OF REDWOOD CITY
INVESTMENT POLICY

Investments under this subdivision shall be rated in a rating category of “AA” or its equivalent or better by an NRSRO and shall not exceed 30% of the City’s moneys that may be invested pursuant to this section. No more than 5% of the City’s portfolio shall be invested in a single issuer.

P. Prohibited Investment Transactions and Derivatives:

1. The Government Code specifically prohibits certain types of investment instruments for municipalities. In addition to those prohibitions, investments not listed under Paragraph IX are not permitted, including, without limitation, the following investments:
 - a. Reverse Repurchase Agreements
 - b. Financial futures or financial option contracts
 - c. Bank Time Deposits
 - d. Security lending
2. Additionally the City shall not invest in any security that could result in zero interest accrual if held to maturity.
3. Due to the complexity of the securities market and ever-changing market conditions, it is difficult to define derivatives and specifically prohibit their acquisition. Therefore, the City desires to limit the potential risk of derivatives by specifically prohibiting the most common types of derivatives with certain market exposures. These prohibited derivatives include but are not limited to: inverse floaters, interest only securities derived from mortgages, residual securities, structured notes, forward based derivatives, forward contracts, forward rate agreements, futures contracts, interest rate futures contracts, foreign currency futures contracts, option based derivatives, option contracts, interest rate caps, interest rate floors, swap contracts, interest rate swaps, interest rate collars, foreign currency swaps, cross currency exchange agreements, fixed rate currency swaps, basis swaps, equity swaps, fixed rate equity swaps, floating rate equity swaps and commodity swaps.
4. Leveraging
 - a. The City may not purchase investments on a margin or through a margin account.
 - b. The General Portfolio may not be leveraged by more than 30% through the issuance of tax and revenue anticipation notes (TRANS). The proceeds of any TRANS issue are to be invested in accordance with the guidelines in this policy, with investment maturities not to exceed the life of the TRANS.
 - c. The City may not leverage its investments through the use of reverse repurchase agreements.

X. Review of Investment Portfolio

The securities held by the City must be in compliance with the authorized investments in this policy at the time of purchase. Because some securities may not comply with this policy subsequent to the date of purchase, the Treasurer shall at least quarterly review the portfolio to identify those securities that do not comply. The Treasurer shall establish procedures to report to the City Council and or the Finance/Audit Sub-Committee major and critical incidences of noncompliance identified through the review of the portfolio.

CITY OF REDWOOD CITY
INVESTMENT POLICY

XI. Investment Pools

A review of Investment Pool policies and procedures is required prior to investing, and on an annual basis.

XII. Collateralization

- A. Bank Deposits: Under provisions of Best Practices, California banks and savings and loan associations are recommended to secure the City's deposits by pledging government securities with a value of 110% of principal and accrued interest or secure City deposits by pledging first trust deed mortgage notes having a value of 150% of the City's total deposits.
- B. Certificates of Deposit:
 - 1. The market value of securities that underlay certificates of deposit shall be valued at 110% of the market value of principal and accrued interest.
 - 2. The City Treasurer, at his/her discretion may waive the collateral requirement for deposits up to the maximum dollar amount which are covered by the Federal Deposit Insurance Corporation.
- C. Repurchase Agreements
 - 1. The market value of securities that collateralize the investment shall be valued at 102% of the market value of principal and accrued interest.
 - 2. The value shall be adjusted no less than weekly. Since the market value of the underlying securities is subject to daily market fluctuations, the investments in repurchase agreements shall be in compliance if the value of the underlying securities is brought back to 102% no later than the next business day.
- D. A clearly marked evidence of ownership, safekeeping receipt, must be supplied to the City and retained.
- E. The City chooses to limit collateral to US Treasuries.
- F. Collateral will always be held by an independent third-party with whom the entity has a current written custodial agreement.
- G. The right of collateral substitution is granted based on the approval of the City Treasurer.

XIII. Safekeeping, Custody and Competitive Bids

- A. Third-party safekeeping is required for all investments. Securities may be maintained by a banking institution or a broker/dealer firm for safekeeping as long as the securities are held in the City's name.
- B. Third-party safekeeping arrangements will be approved by the City Treasurer and will be corroborated by a written custodial agreement.
- C. All investment transactions of the City will be conducted using standard delivery vs. payment

CITY OF REDWOOD CITY
INVESTMENT POLICY

(DVP) procedures.

- D. All securities held by the safekeeping custodian on behalf of the City shall have the City of Redwood City as the registered owner, and all interest and principal payments and withdrawals shall indicate the City of Redwood City as the payee.
- E. All bank deposits will be FDIC insured or deposited with institutions that comply with the State collateral requirements for public funds.
- F. Securities used as collateral for repurchase agreements with a maturity from one to seven days can be held in safekeeping by a third-party bank trust department or by the broker/dealer's safekeeping institution, acting as the agent for the City, under the terms of a custody agreement executed by the selling institution and by the City specifying the City's right to the collateral.
- G. All investment transactions shall be conducted on a competitive basis with quotes from a minimum of two brokers or financial institutions when possible.

XIV. Diversification and Credit Risk Management

- A. Investments contained within the portfolio will be diversified by security type, institution and maturity.
- B. The diversification requirements included in Section IX are designed to mitigate credit risk in the portfolio.
- C. 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. For some investment types, a more restrictive limit is specified in the policy.
- D. 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 City's risk preferences.
- E. If securities owned by the City are downgraded by any nationally recognized statistical ratings organization to a level below the quality required by this Investment Policy, it shall be the City's policy to review the credit situation and make a determination as to whether to sell or retain such securities in the portfolio.
 - 1. If a security is downgraded, the City Treasurer will use discretion in determining whether to sell or hold the security based on its current maturity, the economic outlook for the issuer, and other relevant factors.
 - 2. If a decision is made to retain a downgraded security in the portfolio, its presence in the portfolio will be monitored and highlighted in the quarterly investment report.

XV. Maximum Maturities

- A. The City Treasurer will maintain sufficient liquidity in cash and short-term investments, which together with projected revenue receipts will meet the cash flow requirements of the City for

CITY OF REDWOOD CITY
INVESTMENT POLICY

the upcoming six months.

- B. The City will not directly invest in securities maturing more than five years away from the settlement date. In any case, where a cash flow is matched with an investment which exceeds the five year limit, the investment must be approved by the City Council.
- C. The weighted average maturity of the general portfolio shall not exceed three years. The general portfolio does not include bond proceeds or deferred compensation funds.
- D. To the extent possible, longer-term investment maturities will be spaced so that a portion of such investments mature each year to cover unanticipated emergencies.

XVI. Performance Standards

- A. The investment portfolio shall be designed with the objective of obtaining a rate of return throughout budgetary and economic cycles, commensurate with the investment risk constraints.
- B. The investment performance objective for the portfolio shall be to earn a total rate of return over a market cycle which is approximately equal to the return on a market benchmark index of similar securities, as determined by the City Treasurer.
- C. Market Return (Benchmark): The basis used by the Treasurer to determine whether market return is being achieved shall be to identify a benchmark which reflects a portfolio structure that is comparable to the City's portfolio (An example as it pertains to the long term portion of the portfolio would be the Bank of America Merrill Lynch Index of 1 to 5 Year Government securities).

XVII. Investment Procedures

- A. The City Treasurer shall establish internal procedures for the operation of the investment program consistent with this policy. These procedures shall include, but are not limited to, the following items:
 - 1. Safekeeping
 - 2. Master repurchase agreements
 - 3. Wire transfer agreements
 - 4. Collateral/Depository agreements
 - 5. Broker/Dealer relationships
 - 6. Cash handling, cash management, and accounting practices
- B. 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.
- C. Allocation of Pool Interest
 - 1. All interest earnings related to the investment pool will be allocated to the General Fund unless specifically directed by Federal or State statute, City Council directive, or contractual agreement.

CITY OF REDWOOD CITY
INVESTMENT POLICY

2. The allocation methodology will be maintained by the City Treasurer.

XVIII. Reporting

- A. The City Treasurer will provide a quarterly report to the City Manager and City Council which will include the following information by security, as applicable, held at the end of the reporting period:
 1. Investment Type/Description
 2. Issuer
 3. Purchase Date
 4. Maturity and Call Dates
 5. Book Value/Purchase Price
 6. Par Value
 7. Market Value
 8. Yield by Security and Weighted Average
 9. Source of Market Valuation
 10. Weighted Average Maturity
 11. Funds, investments and loans, if any, that are under the management of contracted parties
 12. Un-invested cash balances
 13. A description of the compliance with the statement of investment policy, or an explanation of any non-compliance.
 14. A statement denoting the ability of the City to meet cash flow requirements for the next six months, or provide an explanation as to why sufficient money shall, or may, not be available.

XIX. Investment Policy Adoption

The City's investment policy shall be adopted by motion of the City Council, who shall also review the policy annually and approve any modification thereto.

XX. Indemnification of Investment Officials

Investment officers acting in accordance with this Policy and written procedures, and reporting and taking appropriate action regarding any adverse developments in a timely manner, will not be held personally liable for any investment losses.

XXI. Glossary of Common Treasury Terminology

AGENCIES: Federal agency securities and/or Government-sponsored enterprises.

ASKED: The price at which securities are offered.

BANKERS' ACCEPTANCE (BA): A draft or bill of exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the issuer.

BENCHMARK: A comparative base for measuring the performance or risk tolerance of the investment portfolio. A benchmark should represent a close correlation to the level of risk and the average duration of the portfolio's investments.

CITY OF REDWOOD CITY

INVESTMENT POLICY

BID: The price offered by a buyer of securities. (When you are selling securities, you ask for a bid.) See Offer.

BROKER: A broker brings buyers and sellers together for a commission.

CERTIFICATE OF DEPOSIT (CD): A time deposit with a specific maturity evidenced by a Certificate. Large-denomination CD's are typically negotiable.

COLLATERAL: Securities, evidence of deposit or other property, which a borrower pledges to secure repayment of a loan. Also refers to securities pledged by a bank to secure deposits of public monies.

COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR): The official annual report of the City. It includes basic financial statements for each individual fund prepared in conformity with Generally Accepted Accounting Principles (GAAP). It also includes supporting schedules necessary to demonstrate compliance with finance-related legal and contractual provisions, extensive introductory material, and a detailed Statistical Section.

COUPON: (a) The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value. (b) A certificate attached to a bond evidencing interest due on a payment date.

DEALER: A dealer, as opposed to a broker, acts as a principal in all transactions, buying and selling for his own account.

DEBENTURE: A bond secured only by the general credit of the issuer.

DELIVERY VERSUS PAYMENT: There are two methods of delivery of securities: delivery versus payment and delivery versus receipt. Delivery versus payment is delivery of securities with an exchange of money for the securities. Delivery versus receipt is delivery of securities with an exchange of a signed receipt for the securities.

DERIVATIVES: (1) Financial instruments whose return profile is linked to, or derived from, the movement of one or more underlying index or security, and may include a leveraging factor, or (2) financial contracts based upon notional amounts whose value is derived from an underlying index or security (interest rates, foreign exchange rates, equities or commodities).

DISCOUNT: The difference between the cost price of a security and its 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:** Non-interest bearing money market instruments that are issued at a discount and redeemed at maturity for full face value (*e.g., U.S. Treasury Bills.*)

DIVERSIFICATION: Dividing investment funds among a variety of securities offering independent returns.

DURATION: A measure of the sensitivity of the price (the value of principal) of a fixed-income investment to a change in interest rates. Duration is expressed as a number of years. Rising interest rates mean falling bond prices, while declining interest rates mean rising bond prices.

FEDERAL CREDIT AGENCIES: Agencies of the Federal government set up to supply credit to various classes of institutions and individuals, *e.g.,* S&L's, small business firms, students, farmers, farm cooperatives, and exporters.

FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC): A federal agency that insures bank deposits, currently up to \$250,000 per entity.

FEDERAL FUNDS RATE: The rate of interest at which Fed funds are traded. This rate is currently pegged by the Federal Reserve through open-market operations.

CITY OF REDWOOD CITY

INVESTMENT POLICY

FEDERAL HOME LOAN BANKS (FHLB): Government sponsored wholesale banks (currently 12 regional banks), which lend funds and provide correspondent banking services to member commercial banks, thrift institutions, credit unions and insurance companies. The mission of the FHLBs is to liquefy the housing related assets of its members who must purchase stock in their district Bank.

FEDERAL NATIONAL MORTGAGE ASSOCIATION (FNMA): FNMA, like GNMA was chartered under the Federal National Mortgage Association Charter Act in 1938. FNMA is a federal corporation working under the auspices of the Department of Housing and Urban Development (HUD). 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's securities are also highly liquid and are widely accepted. FNMA assumes and guarantees that all security holders will receive timely payment of principal and interest.

FEDERAL OPEN MARKET COMMITTEE (FOMC): Consists of seven members of the Federal Reserve Board and five of the twelve Federal Reserve Bank Presidents. The President of the New York Federal Reserve Bank is a permanent member, while the other Presidents serve on a rotating basis. The Committee periodically meets to set Federal Reserve guidelines regarding purchases and sales of Government Securities in the open market as a means of influencing the volume of bank credit and money.

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 influencing the volume of bank credit guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loan associations, and other institutions. Security holder is protected by full faith and credit of the U.S. Government. Ginnie Mae securities are backed by the FHA, VA or FHA mortgages. The term "pass-throughs" is often used to describe Ginnie Maes.

LIQUIDITY: A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value. In the money market, a security is said to be liquid if the spread between bid and asked prices is narrow and reasonable size can be done at those quotes. LOCAL GOVERNMENT INVESTMENT POOL (LGIP): The aggregate of all funds from political subdivisions that are placed in the custody of the State Treasurer for investment and reinvestment.

MARKET VALUE: The price at which a security is trading and could presumably be purchased or sold.

MASTER REPURCHASE AGREEMENT: A written contract covering all future transactions between the parties to repurchase—reverse repurchase agreements that establishes each party's rights in the transactions. A master agreement will often specify, among other things, the right of the buyer-lender to liquidate the underlying securities in the event of default by the seller borrower.

MATURITY: The date upon which the principal or stated value of an investment becomes due and payable.

MONEY MARKET: The market in which short-term debt instruments (bills, commercial paper, bankers' acceptances, etc.) are issued and traded.

OFFER: The price asked by a seller of securities. (When you are buying securities, you ask for an offer.) See Asked and Bid.

OPEN MARKET OPERATIONS: Purchases and sales of government and certain other securities in the open market by the New York Federal Reserve Bank as directed by the FOMC in order to influence the volume

CITY OF REDWOOD CITY

INVESTMENT POLICY

of money and credit in the economy. Purchases inject reserves into the bank system and stimulate growth of money and credit; sales have the opposite effect. Open market operations are the Federal Reserve's most important and most flexible monetary policy tool.

PORTFOLIO: Collection of securities held by an investor.

PRIMARY DEALER: A group of government securities dealers who 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: An investment standard. In some states the law requires that a fiduciary, such as a trustee, may invest money only in a list of securities selected by the custody state—the so-called legal list. In other states the trustee may invest in a security if it is one which would be bought by a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital.

QUALIFIED PUBLIC DEPOSITORIES: A financial institution which does not claim exemption from the payment of any sales or compensating use or ad valorem taxes under the laws of this state, which has segregated for the benefit of the commission eligible collateral having a value of not less than its maximum liability and which has been approved by the Public Deposit Protection Commission to hold public deposits.

RATE OF RETURN: The yield obtainable on a security based on its purchase price or its current market price. This may be the amortized yield to maturity on a bond the current income return.

REPURCHASE AGREEMENT (REPO): A holder of securities sells these securities to an investor with an agreement to repurchase them at a fixed price on a fixed date. The security "buyer" in effect lends the "seller" money for the period of the agreement, and the terms of the agreement are structured to compensate him for this.

REVERSE REPURCHASE AGREEMENT (REVERSE REPO): A reverse-repurchase agreement (reverse repo) involves an investor borrowing cash from a financial institution in exchange for securities. The investor agrees to repurchase the securities at a specified date for the same cash value plus an agreed upon interest rate. Although the transaction is similar to a repo, the purpose of entering into a reverse repo is quite different. While a repo is a straightforward investment of public funds, the reverse repo is a borrowing.

SAFEKEEPING: A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank's vaults for protection.

SECONDARY MARKET: A market made for the purchase and sale of outstanding issues following the initial distribution.

SECURITIES & EXCHANGE COMMISSION: Agency created by Congress to protect investors in securities transactions by administering securities legislation.

SEC RULE 15(C)3-1: See Uniform Net Capital Rule.

STRUCTURED NOTES: Notes issued by Government Sponsored Enterprises (FHLB, FNMA, SLMA, etc.) and corporations, which have imbedded options (e.g., call features, step-up coupons, floating rate coupons, derivative-based returns) into their debt structure. Their market performance is impacted by the fluctuation of interest rates, the volatility of the imbedded options and shifts in the shape of the yield curve.

CITY OF REDWOOD CITY
INVESTMENT POLICY

TREASURY BILLS: A non-interest bearing discount security issued by the U.S. Treasury to finance the national debt. Most bills are issued to mature in three months, six months, or one year.

TREASURY BONDS: Long-term coupon-bearing U.S. Treasury securities issued as direct obligations of the U.S. Government and having initial maturities of more than 10 years.

TREASURY NOTES: Medium-term coupon-bearing U.S. Treasury securities issued as direct obligations of the U.S. Government and having initial maturities from two to 10 years.

UNIFORM NET CAPITAL RULE: Securities and Exchange Commission requirement that member firms as well as nonmember broker-dealers in securities maintain a maximum ratio of indebtedness to liquid capital of 15 to 1; also called net capital rule and net capital ratio. Indebtedness covers all money owed to a firm, including margin loans and commitments to purchase securities, one reason new public issues are spread among members of underwriting syndicates. Liquid capital includes cash and assets easily converted into cash.

YIELD: The rate of annual income return on an investment, expressed as a percentage. (a) **INCOME YIELD** is obtained by dividing the current dollar income by the current market price for the security. (b) **NET YIELD** or **YIELD TO MATURITY** is the current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond.