

DEPARTMENT OF FINANCE -- TREASURY DIVISION

**CITY OF PASADENA INVESTMENT POLICY**

**Fiscal Year 2014 - 2015**

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**I. PURPOSE**

This statement is intended to provide guidelines for the prudent investment of the City's temporary idle cash and reserves, and to outline the policies for maximizing the efficiency of the City's cash management system. The ultimate goal is to enhance the economic status of the City while protecting its pooled cash.

**II. OBJECTIVE**

The City's cash management system is designed to accurately monitor and forecast expenditures and revenues, thus enabling the City to invest funds to the fullest possible extent. The City attempts to earn the highest yield obtainable while remaining within the investment criteria established for the safety and liquidity of public funds.

The investment portfolio will be managed in accordance to the parameters specified within this policy. The investment portfolio will be designed to obtain a reasonable market-level rate of return, given budgetary and economic cycles, commensurate with the City's investment risk and cash flow needs. The City's portfolio management approach will be active, allowing periodic restructuring of the investment portfolio to take advantage of current and anticipated rate movements.

**III. POLICY**

As a Charter City, Pasadena operates its temporary pooled idle cash investments as a trustee and under the prudent person rule (Probate Code Section 16040, et seq., formerly set forth in Civil Code Section 2261, et seq.). The prudent person rule governing the standard of care of trustees, generally states, in essence, that:

- a) *The trustee shall administer the trust with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims to accomplish the purposes of the trust as determined from the trust instrument.*
- b) *When investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing trust property, the trustee shall act with the 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 trust and its beneficiaries, that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims to accomplish the purposes of the trust as determined from the trust instrument. In the course of administering the trust pursuant to this standard, individual investments shall be considered as part of an overall investment strategy.*

This affords the City a broad spectrum of investment opportunities as long as the investment is considered prudent and is allowable under current legislation of the State of California (Government Code Section 53600 et seq.). It is the City's full intent, at the time of purchase, to hold all investments until maturity to ensure the return of all invested principal dollars. However, it is realized that market prices of securities will vary depending on economic and interest rate conditions at any point in time. It is further recognized that in a well-diversified investment portfolio, occasional paper losses are inevitable due to economic, bond market or individual security credit analysis and shifts in interest rates.

It is further recognized that even in a well-diversified portfolio, at any particular point in time, when security valuations are impacted by changes in interest rates and economic conditions, that securities may at times be worth less than the original purchase price. Market fluctuations and occasional measured losses may occur and must be considered within the context of overall portfolio return rather than based on the performance of any single security or investment transaction. It is also understood that in the event of the need for a forced liquidation of investments to meet unplanned or unanticipated cash flow demands, a potential loss of investment principal might occur. The prudent and professional management of portfolio risk includes knowingly selling or changing a security to prevent further losses or to incur loss for the intent of improving credit quality or liquidity.

The City Treasurer, the Finance Director and other individuals assigned to manage the investment portfolio, acting within the intent and scope of the investment policy and other written procedures and exercising due diligence, shall be relieved of personal responsibility and liability for securities credit risk or market price changes, provided deviations from expectations are reported in a timely manner and appropriate action is taken to control adverse developments. Criteria for selecting investments in the order of priority are:

### **1. Safety**

The safety and risk associated with an investment refers to the potential for loss of principal, interest or both. Protection of the public funds entrusted to the Treasurer is the paramount criteria used to evaluate the investment instruments available. Safety of principal is the foremost objective of the City of Pasadena. Each investment transaction shall seek to ensure that capital losses are avoided, whether from securities default, broker-dealer default or erosion of market value. The City shall seek to preserve principal by mitigating the two types of risk, credit risk and market risk.

### **2. Liquidity**

This refers to the ability to convert an investment to cash at any moment in time with minimal risk of forfeiting a portion of principal or interest. Liquidity is an essential investment requirement especially in light of the City's need to be able to meet emergency financing demands of the community at any time.

Because the City of Pasadena operates its own electric and water utility and bills monthly for these services, significant cash flow is generated on a daily basis. Historical cash flow trends are compared to current cash flow requirements on an ongoing basis in an effort to ensure that the City's investment portfolio will remain sufficiently liquid to enable the City to meet all reasonable anticipated operating requirements.

### **3. Yield**

Yield is the potential dollar earnings an investment can provide, and sometimes is described as the rate of return. As a general rule, yields tend to mirror the inherent risk and liquidity characteristics of the particular investment and thus can only be evaluated after those investment criteria are satisfied.

## **IV. LENGTH OF MATURITIES**

The City attempts to obtain the highest yield possible when selecting investments, provided that criteria for safety and liquidity are met. Ordinarily, because investments normally carry a positive yield curve, (i.e., longer term investments have higher rates than shorter maturities), the City attempts to stagger its maturities to meet anticipated cash needs in such a way that new investment money can be placed in maturities that carry a higher rate than is available in the short market of 30 days or under. Furthermore, maturities are selected to position the portfolio to anticipate market risks as well as anticipate cash needs of the City, thereby obviating the need for forced liquidation.

The Government code stipulates that no investment shall be made in securities with maturities in excess of five years without express authority from the City's legislative body. The City Treasurer shall not, at any time, invest in securities with stated maturities exceeding five years with the exception of the Power Reserve portfolio and bond reserve funds as authorized in the bond indentures or with the consent of the bond insurers.

**Stranded Investment Reserve Fund**

The City Council authorizes the City Treasurer to invest monies in the Reserve Fund in securities with maturities exceeding five years. The City Treasurer shall strive to maximize the yield in this fund by extending the maturity of the investments and matching them with future cash flow needs.

**V. DELEGATION OF AUTHORITY**

The authority granted by the Pasadena City Council assigns the responsibility of investing idle cash to the City Treasurer who will report to the Director of Finance. In the City Treasurer's absence, the Director of Finance or the Assistant City Treasurer is authorized to initiate investment transactions. The City Council also delegates to the City Treasurer and the Director of Finance the authority to open new bank accounts, investment and cash management accounts, letters of credit and other credit enhancement products, close bank accounts, investment and cash management accounts, and sign all documents related thereto.

**VI. PORTFOLIO EVALUATION AND REPORTING**

Investment performance is continually monitored and evaluated by the City Treasurer. Investment performance statistics and activity reports are reported monthly to the Director of Finance and the City Manager.

The City Treasurer shall review and render monthly and quarterly reports to the City Manager and the Director of Finance. Government Code Section 53646 (b)(1) states that the Treasurer or Chief Fiscal Officer may render quarterly reports to the legislative body of the local agency containing detailed information on all securities, investments, and moneys of the local agency, a statement of compliance of the portfolio with the statement of investment policy, and a statement of the local agency's ability to meet its pool's expenditures for the next six months. By making these reports optional, this Bill does not impose a state-mandated local program but encourages agencies to continue to report. The quarterly report shall incorporate the disclosure requirements of GASB 40 including the portfolio risk disclosure in the following four primary categories:

1. Credit Risk of Investment positions;
2. Concentration Risk;
3. Interest Rate Risk;
4. Foreign Currency Risk.

**VII. QUALIFIED BROKERS/DEALERS**

The City shall transact business only with national or state chartered banks, and with securities broker/dealers. The broker/dealers should be primary dealers licensed by the state as a broker-dealer or from a member of a federally regulated securities exchange, or from a brokerage firm designated as a primary government dealer by the Federal Reserve Bank. The City can also

transact with non-primary broker/dealers upon the City Treasurer's and the Director of Finance's approval. Investment staff shall investigate dealers who wish to do business with the City to determine if they are adequately capitalized, have pending legal action against the firm or the individual broker and make markets in securities appropriate to the City's needs.

The City Treasurer shall annually send a copy of the current investment policy to all broker/dealers approved to do business with the City of Pasadena. Confirmation of receipt of this policy shall be considered evidence that the dealer understands the City's investment policies and intends to sell the City only appropriate investments authorized by this investment policy.

### **VIII. COLLATERAL REQUIREMENTS**

Collateral is required for investments in certificate of deposits and repurchase agreements. In order to reduce market risk, the collateral level will be at least 102% of the market value of principal and accrued interest.

In order to conform with the provisions of the Federal Bankruptcy Code which provides for liquidation of securities held as collateral, securities acceptable as collateral shall be certificates of deposit, commercial paper, eligible banker's acceptances, medium term notes or securities that are the direct obligations of, or are fully guaranteed as to principal and interest by, the United States or any agency of the United States. Mortgage securities and whole loans can also be used as collateral for the repurchase agreements as long as the collateral level is at least 102% of the market value of the principal and accrued interest.

### **IX. 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 trust department, acting as agent for the City under the terms of a custody agreement or PSA agreement (repurchase agreement collateral). All trades executed by a dealer will settle delivery versus payment (DVP) through the City's safekeeping agent.

### **X. AUTHORIZED INVESTMENTS**

The City shall not invest any funds in any security that could result in a zero interest accrual if held to maturity. In addition, the City shall not invest any funds in inverse floaters, range notes or interest only strips that are derived from a pool of mortgages and also common stocks. However, a local agency may hold prohibited instruments until their maturity date. These limitations will not apply to investments in shares of beneficial interest issued by diversified management companies as referenced in subparagraph 11 of this section.

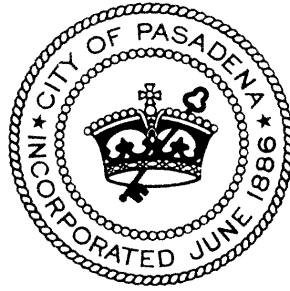
The City is further governed by the California Government Code, Section 53600 et seq. Within the context of these limitations, the following investments are authorized, and further limited herein:

1. United States Treasury Bills, Bonds, and Notes 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 as to the percentage of the portfolio which can be invested in this category, although maturity limitations as stated in Section IV apply.
2. Obligations issued by the Government National Mortgage Association (GNMA), the Federal Farm Credit Bank System (FFCB), the Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Association (FHLMC), the Student Loan Marketing Association (SLMA) and the Tennessee Valley Authority (TVA) and the Federal Home Loan Bank. There is no limitation on the dollar amount that can be invested in these issues except for maturity limitations as stated in Section IV.
3. Bills of exchange or time drafts drawn on and accepted by commercial banks, otherwise known as banker's acceptances. Banker's acceptances purchased may not exceed 180 days to maturity or 40% of the cost value of the portfolio. No more than 30% shall be invested in any one commercial bank pursuant to Section 53601(f) of the Government Code.
4. Commercial paper of "prime" quality of the highest ranking or highest numerical rating as provided for by Moody's Investor services or Standard and Poor's Corporation, and issued by domestic corporations having assets in excess of \$500,000,000 and having an "A" or better rating on its long term debentures as provided by Moody's or Standard & Poor's. Purchases of eligible commercial paper may not exceed 270 days to maturity nor represent more than 10% of the outstanding paper of the issuing corporation. Purchases of commercial paper may not exceed 15% of the cost value of the portfolio. An additional 15%, or a total of 30% of the agency's surplus money, may be invested pursuant to this subdivision. The additional 15% may be so invested only if the dollar weighted average maturity of the entire amount does not exceed 31 days.
5. Negotiable Certificates of Deposit issued by nationally or state chartered banks or state or federal savings institutions. Purchases of negotiable certificates of deposit may not exceed 30% of total portfolio.
6. Investments in Repurchase agreements or securities lending agreements may be made when the term of the agreement does not exceed one year. The market value of the securities used as collateral for the repurchase agreements shall be monitored by the investment staff and shall not be allowed to fall below 102% of the value of the repurchase agreement. A PSA Master Repurchase Agreement is required between the City of Pasadena and the broker dealer or financial Institution for all Repurchase Agreements transacted.
7. Reverse Repurchase Agreements or securities lending agreement which specifies terms and conditions may be transacted with broker/dealers and financial institutions but cannot exceed 20% of the portfolio base value on the date entered into with the conditions as specified in Section 53601(i)(3)(B) of the Government Code.

8. Local Agency Investment Fund (LAIF) which is a State of California managed investment pool may be used up to the maximum permitted by California State Law.
9. Time deposits, non-negotiable and collateralized in accordance with the California Government Code, may be purchased through banks or savings and loan associations. Since time deposits are not liquid, no more than 25% of the investment portfolio may be invested in this investment type.
10. Medium Term Corporate Notes, with a maximum remaining maturity of five years or less may be purchased. Securities eligible for investment shall be rated "A" or better by Moody's or Standard and Poor's rating services. Purchase of medium term notes may not exceed 30% of the cost value of the portfolio and no more than 5% of the cost value of the portfolio may be invested in notes issued by one corporation. Commercial paper holdings should also be included when calculating the 5% limitation.
11. Shares of beneficial interest issued by diversified management companies investing in the securities and obligations as authorized by subdivisions (a) to (j) inclusive of the Government Section or subdivision (m) or (n) and that comply with the investment restrictions of this article and Article 2 (commencing with Section 53630). To be eligible for investment pursuant to this subdivision, these companies shall either:
  - a) Attain the highest ranking or the highest letter and numerical rating provided by not less than two of the three largest nationally recognized rating services.
  - b) Retain an investment advisor registered with the Securities and Exchange Commission with no less than five years of experience investing in the securities and obligations as authorized by subdivisions (a) to (j), inclusive, and 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 any commission that these companies may charge and shall not exceed 20 percent of the agency's surplus money that may be invested pursuant to this section. No more than 10% of the portfolio may be invested in any one mutual fund at the date of purchase.
12. Registered state warrants or treasury notes or bonds, 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.
13. Bonds, notes, warrants or other indebtedness of any local agency within this state, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the local agency, or by a department, board, agency, or authority of the local agency including variable rate demand bonds with a daily or weekly put feature and supported by a credit facility.

- 14.** Any mortgage pass-through security, collateralized mortgage obligation mortgage-backed or other pay-through bond, equipment lease-backed certificate, consumer receivable pass-through certificate, or consumer receivable-backed bond of a maximum of five years maturity. Securities eligible for investment under this subdivision shall be issued by an issuer having an "A" or higher rating for the issuer's debt as provided by a nationally recognized rating service and rated in a rating category of "AA" or its equivalent or better by a nationally recognized rating service. Purchase of securities authorized by this subdivision may not exceed 20% of the agency's surplus money that may be invested pursuant to this section.
- 15.** Contracts issued by insurance companies that provide the policyholder with the right to receive a fixed or variable rate of interest and the full return of principal at the maturity date.
- 16.** Notwithstanding anything to the contrary contained in this section, Section 53635 of the Government Code, or any other provision of law, moneys held by a trustee or fiscal agent and pledged to the payment or security of bonds or other indebtedness, or obligations under a lease, installment sale, or other agreement of a local agency, or certificates of participation in those bonds, indebtedness, or lease installment sale, or other agreements, may be invested in accordance with the statutory provisions governing the issuance of those bonds, indebtedness, or lease installment sale, or other agreement, or to the extent not inconsistent therewith, or if there are no specific statutory provisions, in accordance with the ordinance, resolution, indenture, or agreement of the local agency providing for the issuance.
- 17.** Notes, bonds, or other obligations that are at all times secured by a valid first priority security interest in securities of the types listed by Section 53651 as eligible securities for the purpose of securing local agency deposits having a market value at least equal to that required by Section 53652 for the purpose of securing local agency deposits. The securities serving as collateral shall be placed by delivery or book entry into the custody of a trust company or the trust department of a bank which is not affiliated with the issuer of the secured obligation, and the security interest shall be perfected in accordance with requirements of the Uniform Commercial Code or federal regulations applicable to the types of securities in which the security interest is granted.





DEPARTMENT OF FINANCE -- TREASURY DIVISION  
**CITY OF PASADENA INVESTMENT STRATEGY**  
**Fiscal Year 2014 - 2015**

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**I. PURPOSE**

The City's investment strategy is designed to ensure (1) the prudence and efficiency of investments; (2) the accurate monitoring and forecasting of revenues and expenditures; and, (3) the securing of the safety and liquidity of public funds. The City attempts to earn the highest yield obtainable while maintaining compliance to the criteria of the City's Investment Policy. The qualifications are as follow:

1. To secure safety of funds
2. To maintain liquidity of assets
3. Yield or return
4. To monitor deposits from all departments (Float)
5. Compounding of interest
6. To match investment maturities to large expenditures
7. Flexibility to change investments to maximize security and yield
8. To retain full knowledge of investments available to Treasurers
9. To deal only with qualified brokers and banks
10. To insist upon written confirmation of investments and collateral
11. To check with FHLB for sufficiency of collateral if pooled collateral

## **II. FINANCIAL DATA**

Daily economic and financial market data is obtained from the Bloomberg Financial System and financial experts in the field through bankers, brokers, market analysts and periodicals.

## **III. CASH FORECASTS**

Twelve- and eighteen-month cash forecasts are monitored and updated to accurately estimate revenues and expenditures in order to invest funds to the fullest extent possible.

## **IV. MAINTAINING BANK BALANCES**

Active bank balances are kept at adequate levels without jeopardizing good banking relationships.

## **V. PORTFOLIO TESTING**

The City's portfolio is tested on a monthly basis so that legal limits of types of investments are not exceeded.

## **VI. LIQUIDITY OF FUNDS**

Sufficient funds are maintained in overnight liquid investments to meet current and estimated cash flow needs. The City maintains an adequate level of overnight and short term investments to meet any liquidity and cash need at any given day when cash outflow exceeds cash inflow.

## **VII. PORTFOLIO MANAGEMENT**

In managing the City's portfolio, the City Treasurer considers the overnight investment balance along with securities with maturities of 90 days or less as the operating fund for cash flow purposes. This portion of the portfolio is managed to meet the needs of the regular day to day operating expenses of the public body. Safety of principal and liquidity are the primary investment objectives. Income is a secondary objective. Typically the Treasurer maintains an average investment balance of at least \$40 million in this short term liquid portion of the portfolio with a maturity of one week or less.

The balance of the portfolio is invested in securities with longer term maturities representing the surplus funds. This portion of the portfolio is managed with longer term securities as liquidity is not

the primary objective and may include supplementing the short term liquidity portion of the portfolio if necessary. Safety of principal is still the primary objective, but income, competitive return, and liquidity can be secondary objectives.

## **VIII. MANAGEMENT ACTIVITY**

The investment program shall seek to augment returns consistent with the intent of this policy, identified risk limitations and prudent investment principals. These objectives will be achieved by the potential use when appropriate of the following strategies:

### **1) Active Portfolio Management:**

Through active fund and cash flow management, taking advantage of current economic and interest rate trends, the portfolio yield may be enhanced with limited and measurable increases or decreases in risk by extending or reducing the weighted maturity of the total portfolio and/or actively trading a portion of the portfolio to try to achieve higher returns. Realized gains and losses are expected in active portfolio management and thus authorized as part of the program.

### **2) Portfolio Maturity Management:**

When structuring the maturity composition of the portfolio, the City shall evaluate current and expected interest rate yields and necessary cash flow requirements. It is recognized that in normal market conditions, longer maturities produce higher yields. However, the securities with longer maturities also experience greater price fluctuations when the level of interest rates change.

### **3) Security Swaps:**

The City may take advantage of security swap opportunities or simply sell an investment to improve the overall portfolio yield and/or credit risk. Such transactions that improve the portfolio yield and/or reduce credit risk may be selected even if the transactions result in an accounting loss.