Exhibit A

**CITY OF SALINAS**

# INVESTMENT POLICY

## 1) PURPOSE

The purpose of this document is to establish policies and procedures to ensure effective and judicious management of the investments of the City of Salinas (“City”).

The City’s investment program will conform to this Investment Policy and all applicable federal and state legal requirements, including California Government Code (“Government Code”) Sections 16429.1 et seq. and 53600 et seq.

This Investment Policy replaces any previous investment policy or investment procedures of the City.

## 2) SCOPE

This Investment Policy applies to all financial assets and investment activities of the City and the Successor Agency with the following exception(s):

> Proceeds of debt issuance shall be invested in accordance with the City’s general investment philosophy as set forth in this policy; however, such proceeds are invested in accordance with permitted investment provisions of their specific bond indentures.

*Pooling of funds*: Except for cash in certain restricted and special funds, the City will consolidate cash and reserve balances from all funds to maximize investment earnings and to increase efficiencies with regard to investment pricing, safekeeping, and administration. Investment income will be allocated to the various funds of the City based on their respective invested assets and in accordance with generally accepted accounting principles.

## 3) OBJECTIVES

The City has a fiduciary responsibility to maximize the productive use of all assets entrusted to its care and to invest and manage those public funds wisely and prudently. Therefore, the City shall strive to maintain the level of investment of all idle funds as near 100% as possible through projected cash flow determinations, investing in those investment vehicles deemed prudent and allowable under the laws of the State of California and the ordinances of the City of Salinas.

The objectives of the City’s investment program are, in order, safety, liquidity, and return.

1. *Safety*: Preservation of principal is the foremost objective of the City’s investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio.

2. *Liquidity*: The City's investment portfolio shall remain sufficiently liquid to allow the City to meet all operating requirements which may be reasonably anticipated.
3. *Return*: The City's investment portfolio shall be managed with the objective of attaining a market average rate of return through budgetary and economic cycles, taking into account the City's safety constraints and liquidity requirements and state and local law, ordinances, and resolutions that restrict the placement of short-term funds.

## 4) PRUDENT INVESTOR STANDARD

*Prudent Investor Standard*: Management of the City's investments is governed by the Prudent Investor Standard as set forth in Government Code Section 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."

## 5) PERFORMANCE EVALUATION

Investment performance is to be continually monitored and evaluated by the Finance Director. The City's primary portfolio performance will be measured against an objective index with similar attributes to the City's portfolio.

## 6) DELEGATION OF AUTHORITY

Authority to manage the City's investment program is derived from Government Code Section 53600 et seq. The City Council is responsible for the administration of this Investment Policy. Pursuant to Section 12-5.1 of the Salinas Municipal Code, the City Council has delegated investment authority to the Finance Director. The City Council may renew the delegation of authority each year.

No person may engage in an investment transaction except as provided under the terms of the policy and the procedures established by the Finance Director.

The City may engage the services of one or more external investment managers to assist in the management of the City's investment portfolio in a manner consistent with this Investment Policy and the City's objectives. Such external managers may be granted discretion to purchase and sell investment securities in accordance with this Investment Policy. In accordance with the Investment Advisors Act of 1940, managers must be registered with the Securities & Exchange Commission (SEC) before they can offer their securities in the public market.

The Treasurer and the delegated investment officers, acting in accordance with written procedures and this Investment Policy and exercising due diligence, shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments.

## 7) ETHICS AND CONFLICTS OF INTEREST

Officers and employees involved in the investment process shall refrain from personal business activity that conflicts with proper execution of the investment program or impairs their ability to make impartial investment decisions. In addition, Charter section 8.1 prohibits officers and employees from being directly or indirectly interested in any contract, work or business, the consideration, price or profits of which are payable in whole or in part by the City and from being financially interested, directly or indirectly, in the granting of any franchise, right, or privilege.

## 8) SAFEKEEPING/CUSTODY, DELIVERY, AND COMPETITIVE TRANSACTIONS

A. *Third-Party Safekeeping*: To protect against potential losses by collapse of individual securities dealers, and to enhance access to securities, interest payments and maturity proceeds, all securities owned by the City will be held in safekeeping by a third-party bank custodian, acting as agent for the City under the terms of a custody agreement executed by the bank and the City.

B. *Delivery versus Payment*: Settlement of all investment transactions will be completed on a delivery-versus-payment basis. All securities purchased or acquired shall be delivered to the City of Salinas by book entry, physical delivery, or by third party custodial agreement as required by Government Code Section 53601.

   The only exception to the foregoing shall be depository accounts and securities purchases made with: (i) State of California's Local Agency Investment Fund and other local government investment pools; (ii) non-negotiable certificates of deposit; and, (iii) money market mutual funds, since the purchased securities are not deliverable. Evidence of each these investments will be held by the City.

C. *Competitive Transactions*: All investment transactions will be conducted on a competitive basis which can be executed through a bidding process involving at least three separate brokers/financial institutions where applicable, or through the use of a nationally recognized trading platform.

## 9) DIVERSIFICATION

The City of Salinas will diversify its investments by security type and institution. It is the policy of the City of Salinas to diversify its investment portfolio. Assets shall be diversified to reduce the risk of loss resulting from over concentration of assets in a specific maturity, a specific issuer, or a specific class of securities. Diversification strategies shall be determined and revised periodically and approved by the City Manager and the City Council. In establishing specific diversification strategies, the following general policies and constraints shall apply:

A. Maturities selected shall provide for stability of income and liquidity.

B. Disbursement and payroll dates shall be covered through maturity investments and marketable securities.

## 10) INTERNAL CONTROL

The Finance Director shall establish a system of written internal controls to regulate the City's investment activities, including the activities of any subordinate officials acting on behalf of the City.

The investment portfolio and all related transactions shall be reviewed and balanced to the appropriate general ledger accounts by Department of Finance Staff on a monthly basis.

An independent analysis by the City's external auditor shall be conducted annually as part of the annual audit to review internal control, account activity, and compliance with the Government Code and with policies and procedures and reported to City Council.

## 11) REPORTING

A. The Finance Director shall submit to City Council a quarterly report of investment transactions.

B. The Finance Director shall render a quarterly investment report to the City Manager and City Council.

    1. Except as provided in subsection 2, the quarterly report shall include the following information for each individual investment:

        - type of investment instrument;
        - issuer name;
        - maturity date;
        - par value;

- book value (purchase price);
- current market value and the source of the valuation.

2. For investments placed in the State of California's Local Agency Investment Fund; in FDIC-insured or fully collateralized demand deposit accounts, savings accounts, market rate accounts, time certificates of deposits, and other types of bank deposits in financial institutions located in California; in a county investment pool; or any combination of these, the Finance Director may provide the City Manager and City Council the most recent statement or statements received from these institutions in lieu of the information required by subsection 1 regarding investments in these institutions.
3. The quarterly report also shall (a) state compliance of the portfolio to the statement of Investment Policy, or manner in which the portfolio is not in compliance; (b) include a description of any of the City's funds, investments, or programs that are under the management of contracted parties, including lending programs; and (c) include a statement denoting the ability of the City to meet its expenditure requirements for the next six months, or provide an explanation as to why sufficient money shall, or may, not be available.

C. The Investment Policy shall be reviewed at least annually and, as necessary, adopted by the City Council to ensure its consistency with the overall objectives of safety, liquidity, and return, as well as its relevance to current law and financial and economic trends.

## 12) QUALIFIED BROKER DEALERS

Whenever practical, a competitive bid process will be used for the purchase and sale of investments. It shall be the City's policy to execute investment transactions only with broker/dealers and financial institutions deemed eligible by the Finance Director or the City's Investment Advisor if applicable, will be used to place all investment purchases.

## 13) AUTHORIZED INVESTMENTS

All investments shall be made in accordance with Government Code Sections 16429.1 et seq. and 53600 et seq. Within the investments permitted by the Government Code, the City seeks to further restrict eligible investments to the guidelines listed below. In the event a discrepancy is found between this Investment Policy and the Government Code, the more restrictive parameters will take precedence.

Where this section specifies a percentage limitation for a particular category of investment, that percentage is applicable only at the date of purchase. Where this section does not specify a limitation on the term or remaining maturity at the time of the investment, no investment shall be made in any security, other than a security underlying a repurchase agreement authorized by this section, that at the time of the investment has a term remaining to maturity in excess of five (5) years. Any investment held at the time this Investment Policy is adopted which does not meet the new policy guidelines may be held until maturity and shall be exempt from the current policy. At the time of the investment's maturity or liquidation, such funds shall be reinvested only as provided in the current policy.

A. United States Treasury, notes, bonds, bills, or certificates of indebtedness, or those for which the full faith and credit of the United States are pledged for the payment of principal and interest. There are no limits on the dollar amount or percentage that the City may invest in U.S. Treasuries.

B. 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. No more than 30% of the City's portfolio may be invested in any one federal agency. The maximum percent of agency callable securities in the portfolio will be 20%.

C. Registered state warrants or treasury notes or bonds of the State of California, including bonds payable solely out of revenues from a revenue-producing property owned, controlled, or operated by the state or by a department, board, agency, or authority of the state. The securities must be rated in a rating category of "A" or its equivalent or higher by a nationally recognized statistical rating organization (NRSRO). No more than 30% may be invested in this category in combination with registered treasury notes or bonds of any of the other 49 states. No more than 5% of the portfolio may be invested in any single issuer.

D. 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. The securities must be rated in a rating category of "A" or its equivalent or higher by a NRSRO. No more than 30% may be invested in this category in combination with obligations of the State of California, as well as its political subdivisions. No more than 5% of the portfolio may be invested in any single issuer.

E. 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 local agency, or by a department, board, agency, or authority of the local agency. The securities must be rated in a rating category of "A" or its equivalent or higher by a NRSRO. No more than 30% may be invested in this category in combination with obligations of the State of California, as well as its political subdivisions. No more than 5% of the portfolio may be invested in any single issuer.

F. Repurchase Agreements collateralized with securities authorized under Government Code, maintained at a level of at least 102% of the market value of the repurchase agreement. There are no limits on the dollar amount or percentage that the City may invest, provided that:

- securities used as collateral for repurchase agreements will be delivered to an acceptable third-party custodian;
- repurchase agreements are subject to a master repurchase agreement between the City and the provider of the repurchase agreement. The master repurchase agreement will be substantially in the form developed by the Securities Industry and Financial Markets Association (SIFMA);
- the maximum maturity does not exceed ninety-two days.

G. Reverse repurchase agreements or securities lending agreements may be utilized only when all the following conditions are met:

1. the security to be sold on reverse repurchase agreement or securities lending agreement has been owned and fully paid for by the City for a minimum of 30 days prior to sale;
2. the total of all reverse repurchase agreements and securities lending agreements on investments owned by the City does not exceed 20 percent of the market value of the portfolio;
3. the agreement does not exceed a term of 92 days, unless the agreement includes a written codicil guaranteeing a minimum earning or spread for the entire period between the sale of a security using a reverse repurchase agreement or securities lending agreement and the final maturity date of the same security;
4. funds obtained or funds within the pool of an equivalent amount to that obtained from selling a security to a counterparty by way of a reverse repurchase agreement or securities lending agreement shall not be used to purchase another security with a maturity longer than 92 days from the initial settlement date of the reverse repurchase agreement or securities lending agreement, unless the reverse repurchase agreement or securities lending agreement includes a written codicil guaranteeing a minimum earning or spread for the entire period between the sale of a security using a reverse repurchase agreement or securities lending agreement and the final maturity date of the same security.

Investments in reverse repurchase agreements, securities lending agreements, or similar investments in which the City sells securities prior to purchase with a simultaneous agreement to repurchase the security may only be made upon prior approval of the City Council and shall only be made with primary dealers of the Federal Reserve Bank of New York or with a nationally or state-chartered bank that has or has had a significant banking relationship with the City. The City may not invest more than 20% of its portfolio in reverse repurchase agreements and must always match its maturities to the reinvestment.

H. Bankers' 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 or 40% of the City's surplus moneys that may be invested pursuant to this section. However, no more than 30% of the City's surplus moneys may be invested in the bankers' acceptances of any one commercial bank. Eligible bankers' acceptances are restricted to issuing financial institutions with short-term paper rated in a rating category of “A-1” or its equivalent or higher by a NRSRO or long-term debt obligations rated in a rating category of “A” or its equivalent or higher by a NRSRO.

I. Commercial paper of “prime” quality 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 the following conditions in either paragraph (1) or paragraph (2) below:

   1. The entity meets the following criteria: (a) is organized and operating in the United States as a general corporation, (b) has total assets in excess of five hundred million dollars ($500,000,000), and (c) has debt other than commercial paper, if any, rated in a rating category of “A” or its equivalent or higher by a NRSRO.
   2. The entity meets the following criteria: (a) is organized within the United States as a special purpose corporation, trust, or limited liability company, (b) has program-wide credit enhancements, including, but not limited to, overcollateralization, letters of credit, or surety bonds. (c) has commercial paper rated “A-1” or its equivalent or higher 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 its surplus moneys that may be invested pursuant to this section in eligible commercial paper, and the City may invest no more than 10% of its total investment assets in the commercial paper and the medium-term notes of any single issuer. Under a provision sunsetting on January 1, 2026, no more than 40% of the City’s surplus moneys may be invested in commercial paper if the City’s investment assets under management are greater than $100,000,000. The City may invest no more than 5% of its total investment assets in any single issuer.

J. Medium-term notes 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 subsection must be rated in a rating category of “A” or its equivalent or higher by a NRSRO. Purchases of medium-term notes shall not exceed 30% of the City’s surplus moneys that may be invested pursuant to this section, and the City may invest no more than 5% of its total investment assets in the commercial paper and the medium-term notes of any single issuer.

K. FDIC-insured or fully collateralized demand deposit accounts, savings accounts, market rate accounts, time certificates of deposits (TCDs) and other types of bank deposits in financial institutions located in California. The amount on deposit in any financial institution shall not exceed the shareholder’s equity. To be eligible to receive City deposits, the financial institution must have received a minimum overall satisfactory rating, under the Community Redevelopment Act, for meeting the credit needs of California Communities in its most recent evaluation. Bank deposits are required to be collateralized as specified under Government Code Section 53630 et. seq. The Treasurer, at his/her discretion, may waive the collateralization requirements for any portion that is covered by federal deposit insurance. The City shall have a signed agreement with any depository accepting City funds per Government Code Section 53649. There is no limit on the percentage of the portfolio that may be invested in bank deposits. However, a maximum of 30 percent of the portfolio may be invested in TCDs.

L. Negotiable Certificates of Deposit issued by a nationally- or state-chartered bank or a state or federal savings and loan association, a state or federal credit union, or by a federally- or state-licensed branch of a foreign bank. Amounts of negotiable certificates of deposit insured up to the FDIC limit do not require a credit rating. Any amount above the FDIC insured limit must be issued by institutions with short-term debt obligations rated in a rating category of "A-1" or its equivalent or higher by at least one NRSRO, or long-term obligations rated in a rating category of "A" or its equivalent or higher by a NRSRO. Purchases of negotiable certificates of deposit shall not exceed 30% of the City's surplus moneys that may be invested pursuant to this section. No more than 5% of the portfolio may be invested in any single issuer.

M. Certificates of deposit placed through a deposit placement service that meet the requirements under Government Code Section 53601.8. The full amount of each deposit placed and the interest that may accrue on each such deposit shall at all times be insured by the Federal Deposit Insurance Corporation or the National Credit Union Administration. Purchases of certificates of deposit placed through a deposit placement service shall not, in total, exceed 30 percent of the City's surplus moneys that may be invested pursuant to this section.

N. State of California's Local Agency Investment Fund (LAIF). Investment in LAIF may not exceed the amount permitted by LAIF.

O. Shares of beneficial interest issued by a joint powers authority organized pursuant to Government Code Section 6509.7 that invests in the securities and obligations authorized in this section. 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 this section.
   3. The adviser has assets under management in excess of five hundred million dollars ($500,000,000)

   The underlying pool of securities of which the shares are purchased must be rated in a rating category of "AAAm" or its equivalent or higher by a NRSRO.

P. Shares of beneficial interest issued by diversified management companies that are money market funds registered with the SEC under the Investment Company Act of 1940 (15 USC Sec. 80a-1, et seq.). The purchase price of shares shall not exceed 20 percent of the investment portfolio of the City. To be eligible for investment pursuant to this subdivision, these companies shall have either:

1. attained the highest-ranking letter or numerical rating provided by not less than two of the three largest NRSRO or
2. retained an investment advisor registered or exempt from registration with the SEC with not less than five years' experience managing money market mutual funds and with assets under management in excess of $500,000,000.

Q. A 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. Securities eligible for investment under this subsection shall be rated in a rating category of "AA" or its equivalent or higher by an NRSRO. Purchase of securities authorized by this subsection shall not exceed 20 % of the City's surplus moneys that may be invested pursuant to this section. The City may invest no more than 5% of its total investment assets in the asset-backed or commercial mortgage security of any single issuer.

R. Supranational obligations. Issues must be 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 and eligible for purchase and sale within the United States. The securities must be rated in a rating category of "AA" or its equivalent or higher by a NRSRO. No more than 30% of the City's surplus moneys that may be invested pursuant to this section may be invested in this category. The City may invest no more than 10% of its total investment assets in the supranational obligations of any single issuer.

## 14) PROHIBITED INVESTMENTS

Any security type or structure not specifically approved by this policy is hereby specifically prohibited. Security types which are thereby prohibited include, but are not limited to, inverse floaters, derivatives, range notes, interest only strips that are derived from a pool of mortgages, or in any investment that could result in zero interest accrual if held to maturity. Under a provision sunsetting on January 1, 2026, securities backed by the US Government that could result in a zero- or negative-interest accrual if held to maturity are permitted. Trading securities for the sole purpose of speculating on the future direction of interest rates is prohibited. Purchasing or selling securities on margin is prohibited. The use of reverse repurchase agreements, securities lending or any other form of borrowing or leverage is prohibited. The purchase of foreign currency denominated securities is prohibited. Local governments that are not Qualified Institutional Buyers (QIB) as defined by the SEC are prohibited from purchasing Private Placement Securities. The SEC defines a QIB as having at least $100,000,000 in securities owned and invested. The purchase of a security with a forward settlement date exceeding 45 days from the time of the investment is prohibited.

**15) INVESTMENT OF BOND PROCEEDS**

Bond proceeds shall be invested in the securities permitted by the applicable bond documents. If the bond documents are silent as to the permitted investments, bond proceeds will be invested in the securities permitted by this policy. Notwithstanding the other provisions of this policy, the percentage or dollar portfolio limitations listed in elsewhere in this policy do not apply to bond proceeds. In addition to the securities listed in this Policy, bond proceeds may be invested in a structured investment product if approved by the Finance Director.

**16) LEGISLATIVE CHANGES**

Any State of California legislative action that further restricts allowable maturities, investment type or percentage allocations will be deemed to be incorporated into the City of Salinas's investment policy and will supersede any and all applicable language.

**17) INTEREST EARNINGS**

All moneys earned and collected from investments authorized in this policy shall be allocated monthly to various fund accounts based on the pooled cash balance in each fund as a percentage of the entire pooled portfolio.

## Glossary

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

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

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

**California Local Government Debt:** Is bonds, notes, warrants, or other evidences of indebtedness of any local agency within California. California local government debt is a permitted investment under the California Government Code. The Government Code does not specify minimum credit ratings for local government debt in which local agencies may invest.

**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 of 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.

**Annual Comprehensive Financial Report (ACFR):** The official annual report for the City of Salinas. It includes five combine statements for each individual fund and account group prepared in conformity with 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.

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

**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 deposit.

**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.

**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 FHLB 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 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 and 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 US Government. Ginnie Mae securities are backed by the FHA, VA or FmHA mortgages. The term "pass-throughs" is often used to describe Ginnie Maes.

**Issuer:** Any corporation, government unit or financial institution which borrows money through the sale of securities.

**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 Agency Investment Fund (LAIF):** A special fund in the State Treasury which local agencies may use to deposit funds for investment. All interest is distributed to those agencies participating on a proportionate share determined by the amounts deposited and the length of time they are deposited. Interest is paid quarterly via direct deposit to the LAIF account. The State keeps an amount for reasonable costs of making the investments, not to exceed one-quarter of one per cent of the earnings.

**Local Government Investment Pool (LGIP):** The aggregate of all funds from political subdivisions that are pooled together 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.

**Mutual Funds:** Referred to in the Government Code, Section 53601(l) as "shares of beneficial interest issued by diversified management companies." The Mutual Fund must be restricted by its by-laws to the same investments as the local agency by the Government Code. These investments are Treasury issues, Federal Agency issues, State of California and City (within California) debt obligations, Bankers Acceptances, Commercial Paper, Certificates of Deposit, Negotiable Certificates of Deposit, Repurchase Agreements, Reverse Repurchase Agreements, and Medium-Term Corporate Notes. The quality rating and percentage restrictions in each investment category applicable to the local agency also apply to the Mutual Fund.

**Negotiable:** Term used to designate a security, the title to which is transferable by delivery.

**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 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 included Securities & Exchange Commission (SEC) – registered securities broker-dealers, banks, and a few unregulated firms.

**Principal:** Describes the original cost of a security. It represents the amount of capital or money which the investor pays for the investment.

**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 State 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 (RP or 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. Dealers use RP extensively to finance their positions. Exception: When the Fed is said to be doing RP, it is lending money, that is, increasing bank services.

**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.

**Security:** An investment instrument, other than an insurance policy or fixed annuity, issued by a corporation, government, or other organization which offers evidence of debt or equity.

**Securities & Exchange Commission:** Agency created by Congress to protect investors in securities transactions by administering securities legislation.

**SEC Rule 15C3-1:** 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.

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

**Treasury Notes:** Medium-term coupon-bearing US Treasury securities issued as direct obligations of the US Government and having initial maturities from two to ten years.

**Uniform Net Capital Rule:** Securities & Exchange Commission (SEC) 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 member 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.

**CITY OF SALINAS**

**INVESTMENT GUIDELINES AND STRATEGY**

I. GUIDELINES - Guidelines are established to direct and control activities in such a manner that previously established goals are achieved.

1. Investment Transaction. Every investment transaction must be authorized and reviewed by the Finance Director or his/her designee.

2. Pooled Cash. Whenever practical, local agency cash is consolidated into one bank account and invested on a pooled concept basis. Interest earnings are allocated monthly according to month-end cash and investment balances for each fund.

3. Competitive Bids. Purchase and sales of securities are made on the basis of competitive offers and bids when practical.

4. Cash Forecast. The cash flow for the City is analyzed with the receipt of revenues and maturity of investments scheduled so that adequate cash will be available to meet disbursement requirements.

5. Investment Limitations. Security purchases and holdings are maintained within statutory limits imposed by the California Government Code. Current limits are:

   Bankers' Acceptances 40% Section 53601(f)

   Commercial Paper 25% Section 53601(g)

   Negotiable Certificates of Deposit 30% Section 53601(h)

   Medium Term Notes 30% Section 53601(j)

   Money Market Mutual Funds 20% Section 53601(k)

   Asset-Backed/Mortgage-Backed Securities 20% Section 53601(n)

   Federal Agency restriction 60% per Agency Section 14 of Policy

   Local Agency Investment Fund $50,000,000 per Section 14 of Policy

   CAMP no limit per Section 14 of Policy

   Portfolio Maturing within one year 20% per Section 14 of Policy

6. Liquidity. The marketability of a security is considered at the time of purchase, as the security may have to be sold at a later date to meet unanticipated cash demands.

7. Diversification. The portfolio should consist of a mix of various types of securities, issuers, and maturities.

II. STRATEGY - Strategy refers to the ability to manage financial resources in the most advantageous manner.

1. Economic Forecasts. Economic Forecasts are obtained periodically from economists and financial experts through bankers and brokers to assist the Finance Director or his/her designee with the formulation of an investment strategy for the local agency.

2. Implementing Investment Strategy. Investment transactions are executed which conform with anticipated interest rate trends and the current investment strategy plan.

3. Rapport. A close working relationship is maintained with large vendors of the city. The objective is to pinpoint when large disbursements will clear the city's bank account. It is essential for good cash control that such large expenditures be anticipated, estimated as to dollar amount, and communicated to the Finance Director or his/her designee for liquidity planning purposes.

4. Preserve Portfolio Value. Field standards are developed in order to maintain earnings near the market and to preserve the value of the portfolio.

**CITY OF SALINAS**

**INVESTMENT PROCEDURES**
**INTERNAL CONTROL - GUIDELINES**

OBJECTIVES OF INTERNAL CONTROL

Internal control is the plan of organization and all the related systems established by the management's objective of ensuring, as far as practicable:

- The orderly and efficient conduct of its business, including adherence to management policies.
- The safeguarding of assets.
- The prevention or detection of errors and fraud.
- The accuracy and completeness of the accounting records.
- The timely preparation of reliable financial information.

LIMITATIONS OF INTERNAL CONTROL

No internal control system, however elaborate, can by itself guarantee the achievement of management's objectives. Internal control can provide only reasonable assurance that the objectives are met, because of its inherent limitations, including:

- Management's usual requirement that a control be cost-effective.
- The direction of most controls at recurring, rather than unusual, types of transactions.
- Human error due to misunderstanding, carelessness, fatigue, or distraction.
- Potential for collusion that circumvents controls dependent on the segregation of functions.
- Potential for a person responsible for exercising control abusing that responsibility; a responsible staff member could be in a position to override controls which management has set up.

ELEMENTS OF INTERNAL CONTROL

Elements of a system of internal control are the means by which an organization can satisfy the objectives of internal control. These elements are:

1. ORGANIZATION
   Specific responsibility for the performance of duties should be assigned and lines of authority and reporting clearly identified and understood.

2. PERSONNEL
   Personnel should have capabilities commensurate with their responsibilities. Personnel selection and training policies together with the quality and quantity of supervision are thus important.

3. SEGREGATION OF FUNCTIONS
   Segregation of incompatible functions reduces the risk that a person is in a position both to perpetrate and conceal errors or fraud in the normal course of duty. If two parts of a transaction are handled by different people, collusion is necessary to conceal errors or fraud. In particular, the functions that should be considered when evaluating segregation of functions are authorization, execution, recording, custody of assets, and performing reconciliations.

4. AUTHORIZATION
   All transactions should be authorized by an appropriate responsible individual. The responsibilities and limits of authorization should be clearly delineated. The individual or group authorizing a specific transaction or granting general authority for transactions should be in a position commensurate with the nature and significance of the transactions. Delegation of authority to authorize transactions should be handled very carefully.

5. CONTROLS OVER AN ACCOUNTING SYSTEM
   Controls over an accounting system include the procedures, both manual and computerized, carried out independently to ascertain that transactions are complete, valid, authorized, and properly recorded.

**CITY OF SALINAS**

**CASH CONTROLS**

PROCEDURES PERFORMED BY EXTERNAL AUDITORS WITH RESPECT TO CASH RECEIPTS

A. City procedures and controls are reviewed. Some of the system strengths are:

1. Receipts are controlled upon receipt by proper registration devices.
2. Receipts are reconciled on a daily basis.
3. Amounts batched and deposited intact.
4. Bank reconciliations are reviewed.
5. Prompt posting of cash receipt entries in books.
6. Proper approval required for write-offs of customer accounts.
7. Checks are restrictively endorsed upon receipt or when run through cash register.
8. Adequate physical security over cash.
9. Individuals that handle cash do not post to customer account records or process billing statements.
10. Adequate supervision of Finance Department operations.

B. Significant revenues are confirmed directly with payer and compared with City books to make sure amounts are recorded properly.

C. Cash balances are substantiated by confirming all account balances recorded in books. Bank reconciliations are reviewed for propriety and recalculated by the auditor. All significant reconciling items on bank reconciliations are verified as valid reconciling items by proving to subsequent bank statements.

**CITY OF SALINAS**

**SEGREGATION OF RESPONSIBILITIES OF THE TREASURY FUNCTIONS**

| | Function | Responsibility |
|---|---|---|
| 1. | Formal Investment Policy should be: | |
| | Prepared By: | Finance Director |
| | Approved By: | City Council |
| 2. | Develop Investment Strategy | Finance Director or Registered Investment Advisor |
| 3. | Investment Strategy should be approved by | Finance Director |
| 4. | Execution of investment transactions: | |
| | Investments other than LAIF and Deposits | Finance Director or Registered Investment Advisor |
| | Execution of LAIF and Deposit transfers | Finance Director |
| 5. | Timely recording of investment transactions: | |
| | Recording of investment transactions in the City's accounting records | Finance Director |
| 6. | Verification of investment, i.e., match broker confirmation to City's records | Finance Director |
| 7. | Confirmation of LAIF and Bank Wires | Finance Director |
| 8. | Safeguarding of Assets and Records: | |
| | Reconciliation of City's records to bank statements and safekeeping records | Finance Director |

## CITY OF SALINAS

## SEGREGATION OF RESPONSIBILITIES OF THE TREASURY FUNCTIONS (Continued)

| Function | | Responsibility |
|---|---|---|
| 8. | Safeguarding of Assets and Records (continued): | |
| | Annual review of (a) financial institution's financial condition, (b) safety, liquidity, and potential yields of investment instruments. | Finance Director or Registered Investment Advisor |
| 9. | No less than an annual review of investment portfolio as prepared by Senior Accountant and reviewed by Finance Director | Independent Auditors |