

ACCOUNTING AND FINANCE POLICIES AND PROCEDURES MANUAL

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Investment Policy

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Mission Statement

It is the policy of the City of Cathedral City to invest public funds in a manner which will provide the maximum security with best investment return, while meeting the daily cash flow demands of the City and conforming to all state and local statutes governing the investment of public funds.

Purpose

This statement is intended to provide guidelines for the prudent investment of the City of Cathedral City, Cathedral City Redevelopment Agency, and Cathedral City Public Financing Authority (City) funds 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 safeguarding its assets.

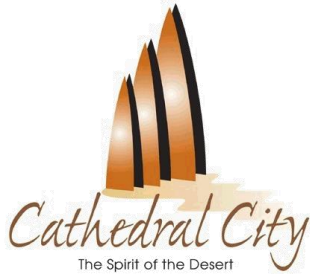
Municipal Code 2.12.040

Pursuant to the delegation of authority in Section 3.08.010, the City Treasurer is authorized to purchase, at their original sale or after they have been issued, securities which are permissible investments under any provision of state law relating to the investing of general city funds, including but not limited to Sections 53601 and 53635 of the Government Code, as said sections now read or may hereafter be amended, from moneys in his custody which are not required for the immediate necessities of the city and as he may deem wise and expedient, and to sell or exchange for other eligible securities and reinvest the proceeds of the securities so purchased. (Ord. 2 § 1 (part), 1981)

Objectives

The primary objectives, in order of priority, of the City's investment activities shall be:

1. **Safety of principal** is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk (the risk of loss due to failure of the financial institution, broker/dealer default, or erosion of market value) and interest rate risk (the risk that the market value of securities in the portfolio will fall due to changes in general interest rates). To attain this objective, the City will diversify its investments by investing funds among a variety of securities offering independent returns and financial institutions.
2. **Liquidity** is the second most important objective of the investment program. The investment portfolio shall remain sufficiently liquid to enable the City to meet all operating and capital requirements that may be reasonably anticipated. Prior to investing City funds, the City Treasurer shall meet with Finance Department staff to understand the City's projected cash needs for day-



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to-day operations and ongoing capital improvement projects. Using this information, the City Treasurer can then determine the appropriate length of time for the investment.

3. **Yield** or rate of return shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles taking into account the investment risk constraints and liquidity needs. Market rate of return is defined as the average return on the one-year U.S. Treasury Bill. Whenever possible, and in a manner consistent with the more important objectives of safety of principal and liquidity, a yield higher than the market rate of return shall be sought.

Standard of Care

The standard of care to be applied shall be the “prudent person,” which states:

Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

Officers and employees acting in accordance with the 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.

Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with the proper execution and management of the investment program, or that could impair their ability to make impartial decisions.

Authority to manage the investment program is granted to the Treasurer, who shall be responsible for the investment of all funds. In his/her absence, the Administrative Services Director and/or Director of Finance, and City Manager, in that order, are authorized to act on his/her behalf. These responsibilities shall include the authority to open accounts with banks, brokers and dealers and to establish safekeeping accounts or other arrangements for the custody of securities and to execute such documents as may be necessary. Prior to any of the above activities being finalized, written concurrence by two of the above individuals shall be obtained.

Responsibility for the operation of the investment program is delegated to the Administrative Services Director and/or Director of Finance, who shall carry out established written procedures and internal controls for the operation of the investment program consistent with this investment policy. Transactions shall be complete, valid, authorized and properly recorded.



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Safekeeping of Securities

All securities owned by the City shall be held in a safekeeping account with the financial institution in the name of the City and under City control at all times. All trades, where applicable, shall be executed by delivery to the City, including those purchased for the City by financial advisers, consultants, or managers by book entry, physical delivery, or by third-party custodial agreement. All security transactions shall be evidenced by safekeeping receipts.

Authorized Investments

Sections 16429.1, 53601, 53601.1, 53601.7, 53635, and 53638 of the Government Code of the State of California set forth the investment vehicles available to local agencies as summarized in the following paragraphs. Section 53601, as now amended, provides that unless Section 53601 specifies a limitation on an investment's maturity, no investments with maturities exceeding five years shall be made unless otherwise directed by the City's Council members.

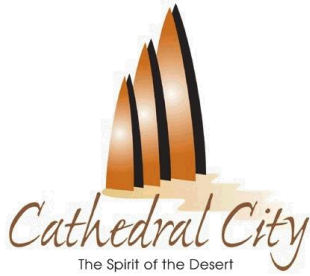
State Treasurer's Local Agency Investment Fund (LAIF) - As authorized in Government Code Section 16429.1 and by LAIF procedures, local government agencies are each authorized to invest a maximum of \$50 million (regular accounts) in this investment program administered by the California State Treasurer. Bond proceeds accounts have no deposit restrictions.

Government Agency Issues - As authorized in Government Code Sections 53601(a) through (f), this category includes a wide variety of government securities which include the following:

- Local government bonds or other indebtedness.
- State bonds or other indebtedness.
- U. S. Treasury notes or other indebtedness secured by the full faith and credit of the federal government.
- Other federal agency securities including but not limited to issues by the Government National Mortgage Association, Federal National Mortgage Association, and the Federal Home Loan Mortgage Corporation.
- State of California obligations such as California Treasury Notes or General Obligation Bonds.

Investment may be made up to 80 percent of the portfolio; however, the total amount may not be committed to any one agency.

Bankers' Acceptances - As authorized in Government Code Section 53601(g), 40 percent of the City's portfolio may be invested in bankers' acceptances, although no more than 30 percent of



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the portfolio may be invested in bankers' acceptances with any one commercial bank. Additionally, the maturity period may not exceed 180 days.

Commercial Paper - As authorized in Government Code Section 53601(h), 25 percent of the City's portfolio may be invested in commercial paper of the highest rating (A-1 or P-1) as rated by Moody's or Standard and Poor's, with maturities not to exceed 270 days. Local agencies may purchase no more than 10 percent of the outstanding commercial paper of any single issuer. There are a number of other qualifications regarding investments in commercial paper based on the financial strength of the corporation and the size of the investment.

Negotiable Certificates of Deposit - As authorized in Government Code Section 53601(i), no more than 30 percent of the agency's money may be invested in 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 state-licensed branch of a foreign bank. All purchases must be fully insured by the FDIC or fully collateralized.

Medium-term notes (MTN's) - As authorized in Government Code Section 53601(k), medium-term notes are defined as all corporate and depository institution debt securities with a maximum remaining maturity of five 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 "A" or better by a nationally recognized ratings service. Purchases of medium-term notes shall not include other instruments authorized by this section and may not exceed 30 percent of the agency's money that may be invested pursuant to this section; however, no more than 5 percent in any one issue or issuer.

Money Market Mutual Funds - As authorized in Government Code Section 53601(l)(2), shares of beneficial interest issued by diversified management companies that are money market mutual funds registered with the Securities and Exchange Commission under the Investment Company Act of 1940. 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 nationally recognized statistical rating organizations; or (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 any commission that the companies may charge and shall not exceed 20 percent of the agency's money that may be invested pursuant to this section. However, no more than 10



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percent of the agency's funds may be invested in shares of beneficial interest of any one mutual fund.

A derivative is defined as a financial instrument created from or whose value depends on the value of one or more underlying assets or indexes of asset values. No investment shall be made in collateralized mortgage obligations (CMO's), interest-only (IO's) and principal-only (PO's) forwards, futures, currency and interest rate swaps, options, and caps/floor/collars. Neither shall any investment be made in reverse repurchase agreements as outlined in Government Code 53601(j).

Diversification of the portfolio will be made in such a manner as to avoid incurring unreasonable risks and with the objectives of this policy at all times. No investment shall be made in a security that is prohibited by this policy or by Government Code 53601.6. Liquidity shall be maintained in such a manner that no less than 20 percent of the portfolio shall have a term of one year or less.

At the time of each investment, either by renewal or initial purchase, an analysis shall be made of the entire portfolio to ensure that the limit for that type of investment shall not be exceeded.

Investments Held by Trustees

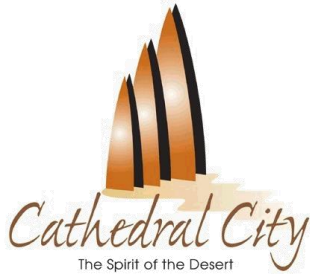
Assets held by fiscal agents are held pursuant to formal agreements such as the requirements of a bond issue or an agreement between the City and another government agency or other entity. The investment of assets held by fiscal agents shall occur pursuant to these formal requirements as permitted by Section 53601(m) of the California Government Code. However, the investment of such assets is subject to the laws established by the State of California pertaining to investments by local agencies as well as the City's primary investment objectives.

Deferred Compensation Plan Assets

Investment decisions regarding these assets are made by the participants pursuant to the deferred compensation plans made available to the City and are not considered a part of this investment policy.

Reporting

Under provisions of the California Government Code Section 53646, there shall be a report at least quarterly made to the City Council and City Manager that reports the status of all investments. Per subdivision (d), the legislative body of a local agency may elect to require the report specified in subdivision (b) to be made on a monthly basis instead of quarterly. The City's Municipal Code requires the City Treasurer to make a monthly report to the City Council of all investments made pursuant to the authority delegated in this chapter. (Municipal Code 3.08.050 – Ord. 2 § 1 (part), 1981)



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These reports shall show for all securities:

- type of investment
- issuer or institution
- date of maturity
- amount of deposit
- rate of interest
- current market value
- accrued interest due
- current broker/dealers and par amount invested through their company as a percentage of the total portfolio

In addition to the items required by Section 53646 of the California Government Code, the following items should be included on the monthly reports to ensure compliance with this investment policy and Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures*:

- investment rating at time of purchase (Moody's / Standard & Poor's)
- investment rating as of June 30 of each fiscal year (Moody's / Standard & Poor's)

Investments held by a fiscal agent and agents for any deferred compensation funds shall be reported based on the most recent published reports received by the City at the time the report is made to the City Council.

Qualified Dealers

The City shall transact investment business only with banks, savings and loans, and registered securities dealers. All financial institutions and broker/dealers who desire to become bidders for investment transactions must supply the City with the following:

- audited financial statements
- proof of National Association of Security Dealers' certification
- trading resolution
- proof of California registration
- certification of having read the City of Cathedral City's investment policy



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- résumé of employees who will be engaged in transactions with the City

A periodic review of the financial condition and registrations of qualified bidders shall be conducted. An annual certification of having read the City's investment policy shall be required by all brokers/dealers.

The Treasurer shall review on a quarterly basis the LAIF report regarding its investments and the market value thereof and obtain and review the State Treasurer's investment policy and annual audited financial report as it pertains to LAIF.

Policy Review

This investment policy shall be reviewed at least annually by the City Council and City Manager or in accordance with California Government Code Section 53646 requirements.

Glossary of Investment Terminology

AGENCIES: Federal agency securities.

AMORTIZED COST: For investments purchased at a discount, amortized cost constitutes cost plus interest earned to date.

ASKED: The price at which securities are offered.

BANKERS' ACCEPTANCE: 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.

BASIS POINT: A basis point equals one one-hundredth of 1% (.01%).

BID: The price offered for securities.

BOOK ENTRY SECURITIES: All U.S. Treasury and Federal Agencies are maintained on computerized records at the Federal Reserve; now known as "wireable" securities.

BROKER: A broker brings buyers and sellers together for a commission paid by the initiator of the transaction or by both sides.

COST: The purchase price of an investment.

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



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CERTIFICATE OF DEPOSIT: A time deposit with a specific maturity evidenced by a certificate. Large-denomination CDs are typically negotiable.

COMMERCIAL PAPER: An unsecured promissory note with a fixed maturity no longer than 270 days. The largest issuers include General Motors Acceptance Corporation (GMAC), General Electric Capital Corporation (GECC) and other major corporations.

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

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.

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

DISCOUNT: The difference between the cost price of a security and its value at maturity when quoted at lower than face value.

DISCOUNT SECURITIES: Securities that are issued at a discount and redeemed at maturity for full face value, e.g., U.S. Treasury bills. Interest is received at maturity.

DIVERSIFICATION: Dividing investment funds among a variety of securities and financial institutions offering.

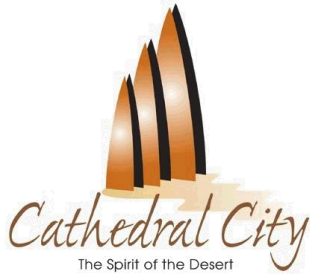
FEDERAL CREDIT AGENCIES: Agencies of the Federal government set up to supply credit to various classes of institutions and individuals, e.g., S & L's, small business firms, students, farmers, farm cooperatives, and exporters.

FEDERAL FUNDS: Non-interest bearing deposits held by member banks at the Federal Reserve.

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

FEDERAL DEPOSIT INSURANCE CORPORATION: A federal agency that insures bank deposits; currently up to \$100,000 per deposit.

FEDERAL HOME LOAN BANKS: The institutions that regulate and lend to savings and loan associations.



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FEDERAL HOME LOAN MORTGAGE CORPORATION (FHLMC): A U.S. Corporation and instrumentality of the U.S. government. Through its purchases of conventional mortgages, it provides liquidity to the mortgage markets, much like FNMA. FHLMC's securities are highly liquid and widely accepted. FHLMC assumes and guarantees that all security holders will receive timely payment of principal and interest.

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 U.S. Department of Housing & Urban Development. 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 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 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.

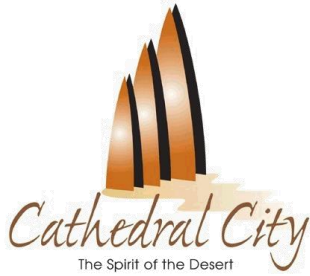
GOVERNMENT NATIONAL MORTGAGE ASSOCIATION (GNMA or Ginnie Mae): Securities guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loans associations and other institutions. Security holder is protected by full faith and credit of the U.S. Government.

LIQUIDITY: A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value.

LOCAL AGENCY INVESTMENT FUND (LAIF): The aggregate of all funds from political subdivisions that are placed in the custody of the State Treasurer for investment.

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.



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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.

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.

PAR VALUE: The amount that will be realized upon maturity of an investment.

PORTFOLIO: Collection of securities held by the investor.

PRIMARY DEALER: A group of government securities dealers that 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.

PRIME RATE: The rate at which banks lend to their best or "prime" customers.

RATE OF RETURN: The yield obtainable on a security based on its purchase price or its current market price.

REPURCHASE AGREEMENT: 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 the buyer for this. Dealers use repurchase agreements extensively to finance their positions.

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

SECONDARY MARKET: A market 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.

SETTLEMENT DATE: The date on which a trade is cleared by delivery of securities against funds. This date may be the same as the trade date or later.



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TRADE DATE: The date on which a transaction is initiated or entered into by the buyer or seller.

TREASURY BILL: A discount security issued by the U.S. Treasury to finance the national debt that matures from three months to one year.

TREASURY BONDS: Long-term U.S. Treasury securities having initial maturities of more than ten years.

TREASURY NOTES: Intermediate term U.S. Treasury securities having initial maturities of from one to ten years.

WHEN-ISSUED TRADES: Typically, there is a delay between the time a new bond is announced and sold, and the time when it is actually issued. During this interval, the security trades “wi”, “when, as, and if issued.”

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 security.