City of Cupertino
Investment Policy
June 6, 2017

POLICY

Under authority granted by the City Council, the City Treasurer and Deputy Treasurer are responsible for investing the surplus funds of the City.

The investment of the funds of the City of Cupertino is directed to the goals of safety, liquidity and yield. The authority governing investments for municipal governments is set forth in the California Government Code, Sections 53601 through 53659.

The primary objective of the investment policy of the City of Cupertino is SAFETY OF PRINCIPAL. Investments shall be placed in those securities as outlined by type and maturity sector in this document. Effective cash flow management and resulting cash investment practices are recognized as essential to good fiscal management and control. The City's portfolio shall be designed and managed in a manner responsive to the public trust and consistent with state and local law. Portfolio management requires continual analysis and as a result the balance between the various investments and maturities may change in order to give the City of Cupertino the optimum combination of necessary liquidity and optimal yield based on cash flow projections.

SCOPE

The investment policy applies to all financial assets of the City of Cupertino as accounted for in the Comprehensive Annual Financial Report (CAFR). Policy statements outlined in this document focus on the City of Cupertino's pooled, surplus funds, but will also apply to all other funds under the City Treasurer's span of control unless specifically exempted by statute or ordinance. This policy is applicable, but not limited to all funds listed below:

- General Fund
- Special Revenue Funds
- Capital Project Funds
- Enterprise Funds
- Internal Service Funds
- Trust and Agency Funds
- Any new fund unless specifically exempted

Investments of bond proceeds shall be governed by the provisions of the related bond indentures and/or cash flow requirements and therefore may extend beyond the maturity limitations as outlined in this document. Other post-employment benefit (OPEB) trust investments are governed by California Government Code Sections 53620 through 53622 and trust documents. The trust is governed by a separate investment policy entitled Investment Policy Statement City of Cupertino Investment Trust that was reviewed by the City of Cupertino Audit Committee and adopted by the City Manager and the Acting Director of Administrative Services on May 6, 2014.

PRUDENCE

The standard to be used by investment officials shall be that of a "prudent person" and shall be applied in the context of managing all aspects of the overall portfolio. Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, direction 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.

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 measured losses are inevitable due to economic, bond market, or individual security valuation fluctuations. These occasional losses must be considered within the context of the overall investment program objectives and the resultant long-term rate of return.

The City Treasurer and Deputy Treasurer, 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 an individual security's 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.

OBJECTIVES

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

A. Safety of Principal

Safety of principal is the foremost objective of the City of Cupertino. Each investment transaction shall seek to ensure that capital losses are avoided, whether from issuer 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.

Credit risk, defined as the risk of loss due to failure of the issuer of a security, shall be mitigated by investing in investment grade securities and by diversifying the investment portfolio so that the failure of any one issuer does not unduly harm the City's capital base and cash flow.

Market risk, defined as market value fluctuations due to overall changes in the general level of interest rates, shall be mitigated by limiting the average maturity of the City's investment portfolio (see maximum maturities) and structuring the portfolio based on historic and current cash flow analysis eliminating the need to sell securities prior to maturity and avoiding the purchase of long term securities for the sole purpose of short term speculation.

B. Liquidity

The City's investment portfolio will remain sufficiently liquid to meet all operating requirements which might be reasonably anticipated and provide the City with adequate cash flows to pay its obligations over the next six months. Additionally, the portfolio should consist largely of securities with active secondary resale markets.

C. Yield

The City's investment portfolio shall be designed with the objective of attaining a rate of return throughout budgetary and economic cycles, commensurate with Cupertino's investment risk constraints and cash flow characteristics of the portfolio.

MAXIMUM MATURITIES

Maturities of investments will be selected based on liquidity requirements to minimize interest rate risk and maximize earnings. Investment of surplus funds shall comply with the maturity limits as set forth in the California Government Code 53600, et seq. 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 that at the time of the investment has a term remaining to maturity in excess of five years, unless the Council has granted express authority to make that investment either specifically or as a part of an investment program approved by the Council no less than three months prior to the investment.

Reserve funds may be invested in securities exceeding five years if the maturity of such investments is made to coincide as nearly as practicable with the expected use of the funds.

PERFORMANCE EVALUATION

Investment performance is continually monitored and evaluated by the City Treasurer. Investment performance statistics and activity reports are generated on a quarterly basis for presentation to the oversight (audit) committee, City Manager and City Council.

Yield on the City's investment portfolio is of secondary importance compared to the safety and liquidity objectives described above. The City's investment portfolio shall be designed to attain a market average rate of return through economic cycles. The market average rate of return is defined as the average return on the Local Agency Investment Fund (assuming the State does not adversely affect LAIF's returns due to budget constraints). Whenever possible, and consistent with risk limitations as defined herein and prudent investment principles, the Treasurer shall seek to augment return above the market average rate of return.

DELEGATION OF AUTHORITY

The Treasurer is responsible for investment management decisions and activities per City Council Resolution.

The Treasurer shall designate a staff person as a liaison/deputy in the event circumstances require timely action and the Treasurer is not present.

No officer or designee may engage in an investment transaction except as provided under terms of this policy and the procedures by the Treasurer and approved by the City Manager/Council.

The Treasurer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

OVERSIGHT COMMITTEE

An audit committee consisting of appropriate internal and external members, appointed by the City Council, shall be established to provide general oversight and direction concerning the policies related to management of the City's investment pool and OPEB trust. The City Treasurer shall serve in a staff and advisory capacity. The committee shall meet at least quarterly to review policy changes, new legislation and portfolio status.

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. Additionally the City Treasurer and the Deputy Treasurer are required to annually file applicable financial disclosures as required by the Fair Political Practices Commission (FPPC).

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 custodian acting as agent for the City under the terms of a custody agreement. All trades executed by a dealer will settle delivery versus payment (DVP) through the City's safekeeping agent.

In order to verify investment holdings, an external auditor, on an annual basis, shall independently verify securities held in custody for the City. Additionally, the City Treasurer shall include a listing of holdings provided by the City's custodian to the quarterly investment report as verification between annual reviews by the external auditor.

All exceptions to this safekeeping policy must be approved by the City Treasurer in written form and included in the quarterly report to City Council.

INTERNAL CONTROL

Separation of duties between the Treasurer's function and Finance is designed to provide proper internal controls to prevent the potential for converting assets or concealing transactions. Dual transaction controls, separate and independent notifications, and reports provided by financial institutions shall be used to help implement these controls.

Wire transfers shall be approved prior to being submitted to the financial institution. Wire transfers initiated by Treasury staff must be reconfirmed by the appropriate financial institution to Finance staff**.** Proper documentation is required for each investment transaction and must include a broker trade confirmation and a cash disbursement wire transfer confirmation. Timely bank reconciliation is conducted to ensure proper handling of all transactions. The investment portfolio and all related transactions are reviewed and balanced to appropriate general ledger accounts by Finance staff on a monthly basis.

An annual agreed-upon procedures engagement in accordance with the attestation standards established by the American Institute of Certified Public Accountants shall be conducted by an auditor solely to assist management in determining the City's compliance with this investment policy. At the conclusion of such engagement, the agreed-upon procedures report detailing all procedures performed and findings noted (if applicable) shall be provided to the Audit Committee of the City.

REPORTING

The City Treasurer shall prepare a quarterly investment report, including a succinct management summary that provides a clear picture of the status of the current investment portfolio. The report will be prepared in a manner that will report all information required under this policy and the California Government Code. The Treasurer will submit the report to Council no later than the second regular council meeting, or approximately 45 days following the end of the quarter covered by the report.

Following its annual or interim adoption by the City Council, this investment policy shall be remitted to the California Debt and Investment Advisory Commission.

QUALIFIED BROKER/DEALERS

Minimum eligibility criteria for dealers/brokers include a minimum of $1 billion in assets and a minimum of five years in business. The registration status of all dealers is checked with the National Association of Securities Dealers.

Dealers are required to acknowledge the receipt and review of the Statement of Investment Policy, to be familiar with the government code restrictions, and have experience with dealing with other municipal investors. Dealers are then selected on the basis of yields, services offered, and references obtained. They may be primary or secondary dealers. The financial institutions must submit a current annual audited financial statement to ascertain capital adequacy.

COLLATERAL REQUIREMENTS

Collateral is required for investments in certificates of deposit and repurchase agreements. In order to reduce market risk, the collateral level will be at least 102% of 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, the only 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.

AUTHORIZED INVESTMENTS

Investment of City funds is governed by the California Government Code Sections 53600 et seq. Within the context of the limitations, the following investments are authorized, as 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 percentage limitation of the portfolio that can be invested in this category, although a five-year maturity limitation is applicable.

2. Obligations issued by the Government National Mortgage Association (GNMA), the Federal Farm Credit System (FFCB), the Federal Home Loan Bank Board (FHLB), the Federal National Mortgage Association (FNMA), the Student Loan Marketing Association (SLMA), and the Federal Home Loan Mortgage Association (FHLMC). There is no percentage limitation of the portfolio that can be invested in this category. A five-year maturity limitation is applicable.

3. Banker's Acceptances (bills of exchange or time drafts drawn on and accepted by commercial banks) may not exceed 180 days to maturity or 40% of the cost value of the portfolio.

4. 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. Investment officers will review LAIF's investment policy, investment mix, rate of return, etc. on a monthly basis.

Investments detailed in items 5 through 10 are further restricted to percentage of the cost value of the portfolio in any one-issuer name to a maximum of 10%. The total value invested in any one issuer shall not exceed 5% of the issuer's net worth. Again, a five-year maximum maturity limitation is applicable unless further restricted by this policy.

5. Commercial paper ranked P1 by Moody's Investor Services or A1+ by Standard & Poor's, and issued by domestic corporations having assets in excess of $500,000,000 and having an AA 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 25% of the cost value of the portfolio.

6. Negotiable Certificates of Deposits issued by nationally or state chartered banks, state or federal savings institutions, or state or federal credit unions. These institutions may use a private sector entity to assist in the placement of the certificates of deposit under the conditions specified by the Government Code. Purchases of Negotiable Certificates of Deposit may not exceed 30% of the cost value of the portfolio. A maturity limitation of five years is applicable.

7. Repurchase agreements that specify terms and conditions may be transacted with banks and broker dealers. The maturity of the repurchase agreements shall 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 Cupertino and the broker/dealer or financial institution for all repurchase agreements transacted.

8. Reverse repurchase agreements are not authorized.

9. Certificates of Deposit (time deposits), non-negotiable and collateralized in accordance with the California Government Code, may be purchased through banks, savings and loan associations, or credit unions. Within a limit of 30% of the cost value of the portfolio, these institutions may use a private sector entity to assist in the placement of the time deposits under the conditions specified by the Government Code.

10. Medium Term Corporate Notes issued by corporations organized and operating in the United States with a maximum maturity of five years may be purchased. Securities eligible for investment shall be rated A or better by Moody's or Standard & Poor's rating services. Purchase of medium term notes may not exceed 30% of the cost value of the portfolio.

11. Bonds issued by the local agency, 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.

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

13. Bonds, notes, warrants or other evidences of indebtedness of any local agency within this state.

14. Various daily money market funds administered for or by trustees, paying agents and custodian banks contracted by the City of Cupertino may be purchased as allowed under State of California Government Code. Only funds holding U.S. Treasury obligations, Government agency obligations, or repurchase agreements collateralized by U.S. Treasury or Government agency obligations can be utilized and may not exceed 20% of the cost value of the portfolio.

15. Ineligible investments are those that are not described herein, including but not limited to, common stocks and long-term (over five years in maturity) notes and bonds are prohibited from use in this portfolio. It is noted that special circumstances arise that necessitate the purchase of securities beyond the five-year limitation. On such occasions, requests must be approved by City Council prior to purchase.

DEPOSITS

To be eligible to receive local agency money, a bank, savings association, federal association, or federally insured industrial loan company shall have received an overall rating of not less than "satisfactory" in its most recent evaluation by the appropriate federal financial supervisorial agency of its record of meeting the credit needs of California's communities.

INTEREST EARNINGS

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

POLICY REVIEW

The City of Cupertino's investment policy shall be adopted by resolution of the City Council on an annual basis. This investment policy shall be reviewed at least annually to ensure its consistency with the overall objectives of preservation of principal, liquidity, and yield, and its relevance to current law and financial and economic trends.