

TREASURER'S STATEMENT OF INVESTMENT POLICY

**CITY OF AVALON AND SUCCESSOR AGENCY TO
THE AVALON COMMUNITY IMPROVEMENT
AGENCY**

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CITY OF AVALON and SUCCESSOR AGENCY TO THE AVALON COMMUNITY IMPROVEMENT AGENCY

TREASURER'S STATEMENT OF INVESTMENT POLICY

I. POLICY

It is the policy of the City of Avalon and Successor Agency to the ACIA (hereinafter collectively referred to as "City" or "City of Avalon") to invest public funds in a prudent manner which will provide in the following order; 1) the highest level of safety of funds, along with 2) liquidity of funds in order that daily cash flow demands are met and, finally, that 3) yield or investment return be maximized while conforming to all laws of the State of California regarding the investment of public funds.

In accordance with Section 53646 of the government Code, the Finance Director and City Treasurer will annually render to the City Council a Statement of Investment Policy. The Finance Director, City Treasurer, and City Manager shall review the policy on an annual basis for submission and approval by the City Council.

II. SCOPE

The City/Agency Treasurer (hereinafter referred to as "Treasurer") is authorized to invest the City's funds in accordance with the California Government Code Sections 53601.1, 53602, and 53635. This investment policy applies to all financial assets of the City of Avalon. These funds are accounted for in the City's Comprehensive Annual Financial Report, which includes the following fund types:

- General Fund
- Special Revenue
- Debt Service
- Capital Projects
- Enterprise
- Internal Service
- Trust and Agency
- Any new fund created by the legislative body, unless specifically exempted

All monies entrusted to the Treasurer will be pooled in an actively managed portfolio except for the employee's retirement funds, which are administered separately and

the proceeds of certain debt issues, which are managed and invested by trustees appointed under indenture agreements.

III. PRUDENCE

The actions of the Treasurer in the performance of his or her duties as manager of public funds shall be evaluated using the following prudent person standard applied in the context of managing the overall portfolio:

- 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.
- Investment officers acting in accordance with written procedures and the investment policy 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.

IV. OBJECTIVES

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

A. Safety

Safety of principal is the foremost objective of the investment program. Investments of the City shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The City shall seek to safeguard principal by a careful examination of credit risk and market risk of individual investments.

1. Credit Risk - The chance that an issuer will be unable to make scheduled payments of interest and principal on an outstanding obligation. Another concern for investors is that the market's perceptions of a corporation's credit will cause the market value of a security to fall, even if default is not expected.
2. Market Risk - The chance that the value of a security will decline as interest rates rise. In general, as interest rates fall, prices of fixed income securities rise. Similarly, as interest rates rise, prices fall. Market risk also is referred to

as systematic risk or risk that affects all securities within and asset class similarly.

B. Liquidity

The City investment portfolio will remain sufficiently liquid to enable the City to meet all operating expenditure requirements, which might be reasonably anticipated. In order to maintain liquidity, no more than 50 percent of the portfolio will have maturity in excess of one (1) year.

C. Return on Investment

The City investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the City investment risk constraints and the cash flow characteristics of the portfolio. Whenever possible, consistent with risk limitations and prudent investment principles, the City shall make an effort to achieve returns at the market average rate of return. The market average rate of return is defined as the average return on six month US Treasury Bills.

V. DELEGATION OF AUTHORITY

The Treasurer has been authorized to undertake investment transactions on behalf of the City. This authority shall not pass to the Deputy Treasurer unless specifically authorized in writing by the Treasurer. Although the Treasurer has been authorized to undertake investment transactions, management responsibility for the City's investment program has been delegated to the Finance Department. The only officials authorized to undertake investment transactions on behalf of the City are the Treasurer, Finance Director, and City Manager. The actual disbursement of funds for the placement of individual investments undertaken by these three officials shall be subject to a second party approval by officers authorized to sign City checks and wire transfers: Mayor, City Manager, Chief Administrative Officer, and Certain Department Heads.

The Treasurer is responsible for ensuring compliance with the City's investment policies and for ensuring that strong internal controls are in place through the oversight of the Finance Director.

VI. ETHICS AND CONFLICTS OF INTEREST

Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions. The Treasurer, Finance Director, and all investment employees are required to file annual disclosure statements as required by the Fair Political Practices Commission (FPPC), thus shall disclose to the City Clerk any material financial interests in financial institutions that conduct business within the jurisdiction, and they shall further disclose any large personal financial investment positions that could be related to the performance of the City investment portfolio.

During the course of the year, if there is an event subject to disclosure that could impair the ability of the Treasurer, Finance Director, or any investment employee to make impartial decisions, the City Manager shall be notified in writing within 10 days. All City Council members, Mayor, City Treasurer, Finance Director, and any investment employees are limited on the receipt of honoraria, gifts, and gratuities from advisors, brokers, dealers, bankers, or other persons with whom the City Treasury conducts business. The permitted approved maximum value of these items is \$50.00.

VII. AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS

The City shall transact business only with issuers, banks, savings and loans, and registered investment securities dealers. The purchase of any investment, other than those purchased directly from the issuer, shall be purchased either from an institution licensed by the State of California as a broker/dealer, as defined in Section 25004 of the Corporations Code, who is a member of the National Association of Securities Dealers (NASD), or a member of a Federally regulated securities exchange, a National or State-Chartered Bank, a Federal or State Association (as defined by Section 5102 of the Financial Code), or a brokerage firm designated as a Primary Government Dealer by the Federal Reserve Bank. The Treasurer's staff shall investigate all institutions that wish to do business with the City/Agency, in order to determine if they are adequately capitalized, make markets in securities appropriate to the City/Agency's needs and agree to abide by the conditions set forth in the City of Avalon/Successor Agency to ACIA Investment Policy and provide a current audited financial statement.

The Treasurer will maintain a list of financial institutions authorized to provide investment services to the City.

VIII. AUTHORIZED AND SUITABLE INVESTMENTS

The State of California Government Code Sections 16429.1, 53601, et seq. limits the investment vehicles available to local agencies. The City of Avalon's Investment Policy further restricts the permitted investments to those listed below.

- State Treasurer's Local Agency Investment Fund (LAIF) - Government Code Section 16429.1 authorizes each local government agency to invest a maximum of \$30 million in this investment program administered by the California State Treasurer. Money invested with LAIF is pooled with State money in order to earn the maximum rate of return possible in a manner consistent with sound investment practices. Furthermore, LAIF provides daily liquidity, therefore, there is no final stated maturity for this investment category. Investments in LAIF shall not exceed \$60 million total (\$30 million each for the City and the Successor Agency to ACIA).
- Los Angeles County Investment Pool (LACIP) - Money invested with the Los Angeles County Investment Pool is pooled with County money in order to earn the maximum rate of return possible in a manner consistent with sound investment practices.
- United States Treasury Bills, Notes, and Bonds or those for which the full faith and credit of the United States are pledged for payment of principal and interest. Purchase of this category shall not exceed five years to maturity. There is no percentage limit in this category.
- Federal Government Obligations - The City may invest in Federally sponsored agency securities including obligations issued by the Government National Mortgage Association (GNMA), the Federal Farm Credit Bank System (FFCB), the Federal Home Loan Bank Board (FHLB), the Federal Home Loan Mortgage Corporation (FHLMC), the Student Loan Mortgage Administration (SLMA), and the Federal National Mortgage Association (FNMA)). The "prudent investor" rule shall apply for a single agency name, as U.S. Government backing is implied rather than guaranteed. There is no percentage limitation of the funds that can be invested in this category. Although a five-year maturity limitation is applicable.
- Negotiable Certificates of Deposit (CDs) - 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.

- Municipal Bonds issued by the State of California and other States in accordance with Code Section 53601, to the extent that the principal amount invested in all funds of this type does not exceed Five Hundred Thousand Dollars (\$500,000).
- Money Market Mutual Funds (with \$1 net asset value) - Investments in money market mutual funds, according to 53601(a) and (k) shall, 1) be restricted to those funds that have attained the highest ranking or highest letter and numerical rating provided by not less than two National Recognized Statistical Rating Organizations (NRSROs), 2) retain an investment advisor registered or exempt from registration with the Securities and Exchange Commission with not less than five years experience managing their specific category of fund and have assets under management in excess of \$500,000,000. A further restriction is that the purchase price of shares of the mutual funds shall not exceed fifteen percent (15%) of the local agency's surplus funds.

IX. COLLATERALIZATION

Collateralization will be required on all Demand Accounts and Uninsured Time Deposits. Demand Accounts and Uninsured Time Deposits with banks and savings and loans shall be collateralized in the manner prescribed by law for depositories accepting municipal investment funds.

X. CONFIRMATION

Receipts for confirmation of purchase of authorized securities should include the following information: trade date, par value, rate, price, yield, settlement date, description of securities purchased, agency's name, net amount due, and third party custodial information. These are minimum information requirements.

XI. SAFEKEEPING OF SECURITIES

In accordance with Government Code Section 53601, all securities owned by the City shall be held in safekeeping by the City's custodial bank or a third party bank trust department, acting for the City under the terms of a custody agreement. All

securities will be received and delivered using standard Delivery-Versus Payment procedures, which ensures that securities are deposited with the third party custodian prior to release of funds. A third party custodian as evidenced by safekeeping receipts will hold securities. Investments in LAIF or money market mutual funds are undeliverable and are not subject to delivery or third party safekeeping.

XII. DIVERSIFICATION

The City will diversify its investments by security type and institution. With the exception of US Treasury securities and authorized pools (LAIF and LACIP), no more than 50% of the entity's total investment portfolio will be invested in a single security type or with a single financial institution.

XIII. MAXIMUM MATURITIES

To the extent possible, the City will attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the City will not directly invest in securities matured more than five (5) years from the date of purchase.

XIV. INTERNAL CONTROL

The Treasurer shall establish an annual process of independent review by an external auditor. This review will provide assurances on internal controls through compliance with policies and procedures.

XV. PERFORMANCE STANDARDS

The investment portfolio will be designed to obtain the highest rate, with the greatest security and liquidity consistent with the cash flow requirements of the City, but at no less rate on the date of investment than the rate being paid by the Local Agency Investment Fund (LAIF).

XVI. REPORTING

Under the provision of Section 53464 of the California Government code, the Treasurer shall render a report to the City Council and the City Manager containing detailed information on all securities, investments, and moneys of the City. The report will be submitted on at least a quarterly basis and provided to the City Council within 30 days following the end of the quarter or reporting period.

The report will contain the following information on the Portfolio that is subject to this investment policy:

1. The type of investment, name of the issuer, date of maturity, par and cost in each investment;
2. The weighted average maturity of the investments;
3. Description of any investments, including loans and security lending programs that are under the management of contracted parties;
4. The market value and source of the valuation;
5. A description of the compliance with the statement of investment policy; and
6. A statement denoting the City's ability to meet its anticipated expenditure requirements for the next six (6) months.

XVII. INVESTMENT POLICY AND ADOPTION

The above investment policy is adopted by resolution of the City of Avalon and the Successor Agency to the Avalon Community Improvement Agency. According to Section 53646, the Treasurer shall review the policy on an annual basis and the City Council and the Successor Agency to the Avalon Community Improvement Agency members shall consider at a public meeting and approve any modifications made thereto.

EXHIBIT A

GLOSSARY

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

Bonds - A debt obligation of a firm or public entity. A bond represents the agreement to repay the debt in principal and, typically, in interest on the principal.

Broker - A person or firm that acts as an intermediary by purchasing and selling securities for others rather than for his or its own account.

Cash Flow - A comparison of cash receipts (revenues) to required payments (debt service, operating expenses, etc.).

Certificate of Deposit - A short-term, secured deposit in a financial institution that usually returns principal and interest to the lender at the end of the loan period. Certificates of Deposit (CDs) differ in terms of collateralization and marketability. Those appropriate to the public agency investing include Negotiable Certificates of Deposit and Non-Negotiable Certificates of Deposit.

Collateralization - Process by which a borrower pledges securities, property, or other deposits for the purpose of securing the repayment of a loan and/or security.

Coupon - The annual rate of interest that a bond's issuer promises to pay the bond holder on the bond's face value; a certificate attached to a bond evidencing interest due on a payment date.

Dealer - Someone who acts as a principal in all transactions, including underwriting, buying, and selling securities, including from his/her own account.

Discount - The difference between the par value of a security and the cost of the security, when the cost is below par. Investors purchase securities at a discount when return to the investor (yield) is higher than the stated coupon (interest rate) on the investment.

Diversification - Dividing investment funds among a variety of securities offering independent return.

Federal Credit Agencies - Agencies of the Federal Government set up to supply credit to various classes of institutions and individuals (e.g. savings and loans, small business firms, students, farmers, farm cooperative, and exporters).

Federal deposit Insurance Corporation (FDIC) - A Federal agency that insures bank deposits, currently up to \$250,000 per institution.

Fiduciary - An individual who holds something in trust for another and bears liability for its safekeeping.

Liquidity - The measure of the ability to convert an instrument to cash on a given date at full face or par value.

Local Agency Investment Fund - A voluntary investment fund open to government entities and certain non-profit organizations in California that is managed by the State Treasurer's Office.

Local Government Investment Pool - Investment pools that range from the State Treasurer's Office Local Agency Investment Fund (LAIF) to county pools, to Joint Powers Authorities (JPAs). These funds are not subject to the same SEC rules applicable to money market mutual funds.

Market Value - The price at which a security is trading and presumably could be purchased or sold at a particular point in time.

Maturity - The date on which the principal or stated value of an investment becomes due and payable.

Money Market Mutual Funds - Mutual funds that invest exclusively in short-term money market instruments. MMF's seek the preservation of capital as a primary goal while maintaining a high degree of liquidity and providing income representative of the market for short term investments.

Municipal Notes, Bonds, and Other Obligations - Obligations issued by state and local governments to finance capital and operating expenses.

Mutual Funds - An investment company that pools money and can invest in a variety of securities, including fixed-income securities and money market instruments.

Portfolio - Combined holding of more than one stock, bond, commodity, real estate investment, cash equivalent, or other asset. The purpose of a portfolio is to reduce risk by diversification.

Prudent Person Standard - A standard of conduct where a person acts with care, skill, prudence, and diligence when investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing funds. The test of whether the standard is being met is if a prudent person acting in such a situation would engage in similar conduct to ensure that investments safeguard principal and maintain liquidity.

Rate of Return - For fixed-rate securities, it is the coupon or contractual dividend rate divided by the purchase price, which is also the current yield.

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.

Securities and Exchange Commission (SEC) - The Federal Agency responsible for supervising and regulating the securities industry.

US Treasury Obligations - Debt obligations of the US Government sold by the Treasury Department in the forms of bills, notes, and bonds. Bills are short-term obligations that mature in one year or less and are sold at a discount. Notes are obligations that mature between one year and ten years. Bonds are long-term obligations that generally mature in ten years or more.

Weighted Average Maturity (WAM) - The average maturity of all the securities that comprise a portfolio, typically expressed in days or years.

Yield - The current rate of return on an investment security generally expressed as a percentage of the securities current price.