



TOWN OF
LOS GATOS
CALIFORNIA

COUNCIL POLICY MANUAL

Small Town Service Community Stewardship Future Focus

TITLE: Investment Policy

POLICY NUMBER: 4-02

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APPROVED:

PURPOSE

The Town of Los Gatos (the "Town"), incorporated in 1887, is located approximately 60 miles south of San Francisco, in the southwestern portion of Santa Clara County. The Town operates under the Council/Manager form of government. The Town Council is the legislative body for the Town. It has five members elected to serve staggered four year terms. The Town Manager is appointed by the Town Council.

The Town Council has adopted this Investment Policy in order to establish the investment scope, objectives, delegation of authority, standards of prudence, reporting requirements, internal controls, eligible investments and transactions, diversification requirements, risk tolerance, and safekeeping and custodial procedures for the investment of the funds of the Town. All Town funds will be invested in accordance with this Investment Policy and with applicable sections of the California Government Code.

This Investment Policy was originally adopted by the Town Council of the Town of Los Gatos November 1, 2016. It replaces any previous investment policy or investment procedures of the Town.

SCOPE

This Investment Policy applies to all of the Town's short-term operating funds. These funds are described in the Town's annual financial report and include, but are not limited to:

General Fund

Special Revenue Funds

- Capital Project Funds
- Debt Service Funds
- Enterprise Fund
- Internal Service Funds
- Fiduciary Funds

Specifically excluded from this Investment Policy are amounts which are held by a trustee or fiscal agent and pledged as payment or security for bonds or other indebtedness, obligations under a lease, or

obligations under certificates of participation. Such funds are invested in accordance with statutory provisions, ordinance, resolution, or indenture governing the issuance of the obligations. In addition, this Investment Policy is not applicable to the Town's Deferred Compensation Plan. These investments are directed by each employee participant in accordance with the rules of the Deferred Compensation Plan.

POLICY

OBJECTIVES

The Town's funds shall be invested in accordance with all applicable Town policies and codes, State statutes, and Federal regulations, and in a manner designed to accomplish the following objectives, which are listed in priority order:

1. Preservation of capital and protection of investment principal.
2. Maintenance of sufficient liquidity to meet anticipated cash flows.
3. Attainment of a market value rate of return.
4. Diversification to avoid incurring unreasonable market risks.

DELEGATION OF AUTHORITY

Management responsibility for the Town's investment program is delegated annually by the Town Manager to the Town Treasurer/Finance Director (the "Treasurer") pursuant to California Government Code Section 36510. The Treasurer may delegate the authority to conduct investment transactions and to manage the operation of the investment portfolio to other specifically authorized staff members. The Treasurer shall maintain a list of persons authorized to transact securities business for the Town. No person may engage in an investment transaction except as expressly provided under the terms of this Investment Policy.

The Treasurer shall develop written administrative procedures and internal controls, consistent with this Investment Policy, for the operation of the Town's investment program. Such procedures shall be designed to prevent losses arising from fraud, employee error, misrepresentation by third parties, or imprudent actions by employees.

The Town may engage the support services of outside investment advisors in regard to its investment program, so long as it can be demonstrated that these services produce a net financial advantage or necessary financial protection of the Town's financial resources.

PRUDENCE

The standard of prudence to be used for managing the Town's investments shall be California Government Code Section 53600.3, the prudent investor standard which states, "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.”

The Town's overall investment program shall be designed and managed with a degree of professionalism that is worthy of the public trust. The Town recognizes that no investment is totally without risk and that the investment activities of the Town are a matter of public record. Accordingly, the Town recognizes that occasional measured losses may occur in a diversified portfolio and shall be considered within the context of the overall portfolio's return, provided that adequate diversification has been implemented and that the sale of a security is in the best long-term interest of the Town.

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

ETHICS AND CONFLICTS OF INTEREST

Elected officials and Town employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution of the investment program or could impair or create the appearance of an impairment of their ability to make impartial investment decisions. Elected officials and Town employees shall disclose to the Town Council any business interests they have in financial institutions that conduct business with the Town and they shall subordinate their personal investment transactions to those of the Town. In addition, the Town Manager and the Treasurer shall file a Statement of Economic Interests each year pursuant to California Government Code Section 87203 and regulations of the Fair Political Practices Commission.

AUTHORIZED SECURITIES AND TRANSACTIONS

All investments and deposits of the Town shall be made in accordance with California Government Code Sections 16429.1, 53600-53609 and 53630-53686, except that pursuant to California Government Code Section 5903(e), proceeds of bonds and any moneys set aside or pledged to secure payment of the bonds may be invested in securities or obligations described in the ordinance, resolution, indenture, agreement, or other instrument providing for the issuance of the bonds. Any revisions or extensions of these code sections will be assumed to be part of this Investment Policy immediately upon being enacted. However, in the event that amendments to these sections conflict with this Investment Policy and past Town investment practices, the Town may delay adherence to the new requirements when it is deemed in the best interest of the Town to do so. In such instances, after consultation with the Town's attorney, the Treasurer will present a recommended course of action to the Town Council for approval.

The Town has further restricted the eligible types of securities and transactions as follows:

1. United States Treasury bills, notes, bonds, or certificates with a final maturity not exceeding five years from the date of trade settlement.
2. Federal Agency Obligations for which the faith and credit of the United States are pledged for the payment of principal and interest and which have a final maturity not exceeding five years from the

date of trade settlement. There is no limit on the percentage of the portfolio that can be invested in this category, however, no more than 20% of the town's total portfolio shall be invested in the combination of Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA) and Federal Home Loan Mortgage Corporation (FHLMC) mortgage-backed securities.

3. Federal Instrumentality (government sponsored enterprise) debentures, discount notes, callable securities, step-up securities, and mortgage-backed securities (including FNMA and FHLMC) with a final maturity not exceeding five years from the date of trade settlement. There is no limit on the percentage of the portfolio that can be invested in this category, however, no more than 20% of the town's total portfolio shall be invested in the combination of GNMA, FNMA, and FHLMC mortgage-backed securities.
4. Prime Commercial Paper with a maturity not exceeding 270 days from the date of trade settlement with the highest ranking or of the highest letter and number rating as provided for by a nationally recognized statistical-rating organization (NRSRO). The entity that issues the commercial paper shall meet all of the following conditions in either sub-paragraph A. or sub-paragraph B. below:

A. The entity shall (1) be organized and operating in the United States as a general corporation, (2) have total assets in excess of five hundred million dollars (\$500,000,000) and (3) Have debt other than commercial paper, if any, that is rated "A" or higher by a NRSRO.

B. The entity shall (1) be organized within the United States as a special purpose corporation, trust, or limited liability company, (2) have program wide credit enhancements, including, but not limited to, over collateralization, letters of credit or surety bond and (3) have commercial paper that is rated "A-1" or higher, or the equivalent, by a NRSRO.

Purchases of eligible commercial paper shall not exceed:

- 10% of the outstanding commercial paper of any single corporate issuer,
- 5% of the Town's total portfolio in the commercial paper of any one issuer, and
- 25% of the Town's total portfolio.

5. Eligible Bankers Acceptances with a maturity not exceeding 180 days from the date of trade settlement, issued by a state or national bank with combined capital and surplus of at least \$250 million, whose deposits are insured by the FDIC, and whose senior long-term debt is rated at least A or the equivalent by a NRSRO at the time of purchase. No more than 5% of the Town's total portfolio shall be invested in banker's acceptances of any one issuer, and the aggregate investment in banker's acceptances shall not exceed 30% of the Town's total portfolio.
6. 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, with a final maturity not exceeding five years from the date of trade settlement, and rated at least "A" or the equivalent by a NRSRO. No more than 5% of the Town's total portfolio shall be

invested in the medium-term notes of any one issuer and the aggregate investment in medium term notes shall not exceed 30% of the Town's total portfolio.

7. Municipal & State Obligations:

- A. Municipal bonds including registered notes or bonds of any of the 50 states, 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 50 states.
- B. In addition, bonds, notes, warrants, or other evidences of indebtedness of any local agency in California, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, operated by the local agency, or by a department, board, agency, or authority of the local agency.

Municipal bonds must be rated at least "A" or the equivalent by a NRSRO with maturities not exceeding five years from the date of the trade settlement. No more than 5% of the Town's total portfolio shall be invested in "A" rated bonds or in the bonds of any one municipality. In addition, the aggregate investment in municipal bonds may not exceed 30% of the total portfolio.

8. Certificates of Deposit with a final maturity not exceeding five years from the date of trade settlement. The aggregate investment in certificates of deposit shall not exceed 30% of the Town's portfolio, and no more than 5% of the portfolio shall be held in any one deposit or allocated to any one issuer. Certificates of Deposit shall be issued by a nationally or state-chartered bank or a state or federal savings and loan association or by a state-licensed branch of a foreign bank or by a federally licensed branch of a foreign bank provided that the senior debt obligations of the issuing institution are rated at least "A" or the equivalent by a NRSRO.

Negotiable certificates of deposit issued by a nationally or state-chartered bank, or by a federally licensed or state-licensed branch of a foreign bank. Purchases of negotiable certificates of deposits are subject to the limitations of Section 53601(i), shall be fully insured by the FDIC with a corresponding FDIC certification number, and shall be delivered through the Depository Trust Company.

Non-Negotiable certificates of deposit issued by a nationally or state-chartered bank, or by a federally licensed or state-licensed branch of a foreign bank. Purchases of non-negotiable certificates of deposit are subject to the limitations of Sections 53601(n) and 53638 and shall be fully insured by the FDIC with a corresponding FDIC certification number.

Private sector entities may be used to place certificates of deposit subject to the limitations of Section 53601.8.

9. State of California's Local Agency Investment Fund (LAIF), pursuant to California Government Code Section 16429.1. The aggregate amount invested in LAIF shall not exceed the maximum allowed by the fund.
10. Money Market Funds registered under the Investment Company Act of 1940 that (1) are "no-load" (meaning no commission or fee shall be charged on purchases or sales of shares); (2) have a

constant net asset value per share of \$1.00; (3) invest only in the securities and obligations authorized by applicable California Statute and (4) have a rating of at least AAA or the equivalent by at least two NRSROs. No more than 10% of the Town's total portfolio shall be invested in money market funds of any one issuer, and the aggregate investment in money market funds shall not exceed 20% of the Town's total portfolio.

Securities that have been downgraded to a level that is below the minimum ratings described herein may be sold or held at the Town's discretion. The portfolio will be brought back into compliance with Investment Policy guidelines as soon as is practical.

The foregoing list of authorized securities and transactions shall be strictly interpreted. Any deviation from it must be preapproved by resolution of the Town Council.

PORTFOLIO MATURITIES AND LIQUIDITY

To the extent possible, investments shall be matched with anticipated cash flow requirements and known future liabilities. The Town will not invest in securities maturing more than five years from the date of trade settlement, unless the Town Council has by resolution granted authority to make such an investment at least three months prior to the date of investment.

SELECTION OF BROKER/DEALERS

The Treasurer shall maintain a list of broker/dealers approved for investment purposes, and it shall be the policy of the Town to purchase securities only from those authorized firms. To be eligible, a firm must meet at least one of the following criteria:

- Be recognized as a Primary Dealer by the Federal Reserve Bank of New York or have a primary dealer within their holding company structure; or
- Report voluntarily to the Federal Reserve Bank of New York; or
- Qualify under Securities and Exchange Commission (SEC) Rule 15c3-1 (Uniform Net Capital Rule).

In addition, authorized broker/dealers must be licensed by the State of California as a broker/dealer as defined in Section 25004 of the California Corporations Code.

The Town may engage the services of investment advisory firms to assist in the management of the portfolio and investment advisors may utilize their own list of approved broker/dealers. Such broker/dealers will comply with the selection criteria above and the list of approved firms shall be provided to the Town on an annual basis or upon request.

In the event that an external investment advisor is not used in the process of recommending a particular transaction in the Town's portfolio, authorized broker/dealers shall attest in writing that they have received and reviewed a copy of the this Investment Policy and shall be required to submit and annually update a Town approved Broker/Dealer Information request form, which includes the firm's most recent financial statements.

The Town may purchase commercial paper from direct issuers even though they are not on the approved broker/dealer list as long as they meet the criteria outlined in Item 4 of the Authorized Securities and Transactions section of this Investment Policy.

COMPETITIVE TRANSACTIONS

Each investment transaction shall be competitively transacted with authorized broker/dealers. At least three broker/dealers shall be contacted for each transaction and their bid and offering prices shall be recorded.

If the Town is offered a security for which there is no other readily available competitive offering, the Treasurer will document quotations for comparable or alternative securities.

SELECTION OF BANKS

The Treasurer shall maintain a list of banks and savings banks approved to provide banking services for the Town. To be eligible, a bank must be a member of the Federal Deposit Insurance Corporation, must qualify as a depository of public funds in the State of California as defined in California Government Code Section 53630.5 and shall secure deposits in excess of FDIC coverage in accordance with California Government Code Section 53652.

Authorized banks that accept deposits from the Town shall meet high standards with regard to liquidity, asset quality, profitability and capital adequacy. The Treasurer shall utilize a commercial bank rating service to perform credit analysis on banks seeking authorization. Banks that in the judgment of the Treasurer no longer offer adequate safety to the Town shall be removed from the Town's list of authorized banks.

SAFEKEEPING AND CUSTODY

The Treasurer shall select one or more financial institutions to provide safekeeping and custodial services for the Town. A Safekeeping Agreement shall be executed with each custodian bank prior to utilizing that bank's safekeeping services.

Custodian banks will be selected on the basis of their ability to provide services for the Town's account and the competitive pricing of their safekeeping related services.

The purchase and sale of securities and repurchase agreement transactions shall be settled on a delivery versus payment basis. All securities shall be perfected in the name of the Town. Sufficient evidence to title shall be consistent with modern investment, banking and commercial practices.

All investment securities, purchased by the Town, will be delivered by book entry and will be held in third-party safekeeping by a Town approved custodian bank or its Depository Trust Company (DTC) participant account.

All Fed wireable book entry securities owned by the Town shall be held in the Federal Reserve System in a customer account for the custodian bank which will name the Town as "customer."

All DTC eligible securities shall be held in the custodian bank's DTC participant account and the custodian bank shall provide evidence that the securities are held for the Town as "customer."

PORTFOLIO PERFORMANCE

The investment portfolio shall be designed to attain a market rate of return throughout budgetary and economic cycles, taking into account prevailing market conditions, risk constraints for eligible securities, and cash flow requirements. The performance of the Town's investments shall be compared to the average yield on the U.S. Treasury security that most closely corresponds to the portfolio's weighted average effective maturity. When comparing the performance of the Town's portfolio, its rate of return will be computed net of all fees and expenses.

REPORTING

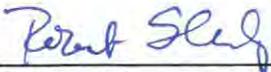
No less than quarterly, the Treasurer shall prepare a report of the investment earnings and performance results of the Town's investment portfolio. The report shall be submitted to the Town Clerk within 45 days after the end of each quarter for inclusion as an agenda item at the next scheduled Town Council meeting. The report shall include the following information:

1. Investment type, issuer, date of maturity, par value and dollar amount invested in all securities, and investments and monies held by the Town;
2. A market value as of the date of the report (or the most recent valuation as to assets not valued monthly) and the source of the valuation;
3. Realized and unrealized gains or losses calculated by amortized cost and by fair value.
4. The weighted average maturity of the portfolio and a percentage breakdown of the total portfolio by maturity.
5. A description of the funds, investments and programs that are under the management of contracted parties;
6. A statement of compliance with this Investment Policy or an explanation for non-compliance; and
7. A statement of the ability to meet expenditure requirements for the next six months, and an explanation of why money will not be available if that is the case.

PROCEDURES

This Investment Policy shall be adopted by resolution of the Town Council. Annually the Town Manger shall present this Investment Policy to the Town Council for review to ensure its consistency with the Town's investment objectives, current law and economic trends. Any amendments to this Investment Policy shall be approved by the Town Council.

APPROVED AS TO FORM:



Robert Schultz, Town Attorney