CITY OF NEWPORT BEACH
FINANCE COMMITTEE AGENDA

Newport Coast Conference Room, Bay 2E
100 Civic Center Drive, Newport Beach
Monday, July 22, 2013 – 4:00 PM

Finance Committee Members:	***Staff Members:***
Mike Henn, Council Member, Chair	Dave Kiff, City Manager
Keith Curry, Mayor	Dan Matusiewicz, Finance Director
Tony Petros, Council Member	Steve Montano, Deputy Finance Director

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1) CALL MEETING TO ORDER

2) ROLL CALL

3) PUBLIC COMMENTS

Public comments are invited on agenda and non-agenda items generally considered to be within the subject matter jurisdiction of the Finance Committee. Speakers must limit comments to 3 minutes. Before speaking, we invite, but do not require, you to state your name for the record. The Finance Committee has the discretion to extend or shorten the speakers' time limit on agenda or non-agenda items, provided the time limit adjustment is applied equally to all speakers. As a courtesy, please turn cell phones off or set them in the silent mode.

4) APPROVAL OF MINUTES

Approval of the June 24, 2013 Finance Committee meeting minutes.

5) CURRENT BUSINESS

A. Investment Policy Review: Staff will present its annual review of the City's investment policy and seek approval and guidance from the Finance Committee regarding the scope, objectives, and standards that govern the City's investment portfolio.

B. Investment Portfolio Review: Staff and/or one or more investment advisors will describe the performance of the City's investment portfolio.

C. Investment Strategy Recommendations: Staff will discuss the merits and reasons for considering an alternative investment portfolio management strategy.

This Finance Committee is subject to the Ralph M. Brown Act. Among other things, the Brown Act requires that the Finance Committee's agenda be posted at least seventy-two (72) hours in advance of each regular meeting and that the public be allowed to comment on agenda items before the Finance Committee and items not on the agenda but are within the subject matter jurisdiction of the Finance Committee. The Finance Committee may limit public comments to a reasonable amount of time, generally three (3) minutes per person.

It is the intention of the City of Newport Beach to comply with the Americans with Disabilities Act ("ADA") in all respects. If, as an attendee or a participant at this meeting, you will need special assistance beyond what is normally provided, the City of Newport Beach will attempt to accommodate you in every reasonable manner. If requested, this agenda will be made available in appropriate alternative formats to persons with a disability, as required by Section 202 of the Americans with Disabilities Act of 1990 (42 U.S.C. Sec. 12132), and the federal rules and regulations adopted in implementation thereof. Please contact the City Clerk's Office at least forty-eight (48) hours prior to the meeting to inform us of your particular needs and to determine if accommodation is feasible at (949) 644-3005 or cityclerk@newportbeachca.gov.

6) **FINANCE COMMITTEE ANNOUNCEMENTS OR MATTERS WHICH MEMBERS WOULD LIKE PLACED ON A FUTURE AGENDA FOR DISCUSSION, ACTION OR REPORT (NON-DISCUSSION ITEM)**

7) **ADJOURNMENT**

CITY OF NEWPORT BEACH
CITY COUNCIL FINANCE COMMITTEE
JUNE 24, 2013 MEETING MINUTES

1. CALL TO ORDER

The meeting was called to order at 4:02 p.m. in the Newport Coast Conference Room, Bay 2E, 100 Civic Center Drive, Newport Beach, California 92660.

2. ROLL CALL

Present: Council Member Mike Henn (Chair), Mayor Keith Curry and Council Member Tony Petros

Staff present: City Manager Dave Kiff, Finance Director Dan Matusiewicz, Deputy Finance Director Steve Montano, Accounting Manager Rukshana Virany, Revenue Manager Evelyn Tseng, Fire Chief Scott Poster, Deputy Chief Kevin Kitch, Lifeguard Operations Assistant Chief Rob Williams, EMS Manager Cathy Ord, Assistant City Attorney Leonie Mulvihill, HR/Risk Manager Lauren Farley and Administrative Coordinator Tammie Frederickson

Outside entities: Nitin Patel, White Nelson Diehl Evans LLP; Erin Payton, MGT of America, Inc.

Members of the public: Jim Mosher, Carl Cassidy

3. PUBLIC COMMENTS

No public comments were made.

4. APPROVAL OF MINUTES

Council Member Petros moved, Mayor Curry seconded to approve the minutes of the May 13, 2013, meeting inclusive of Mr. Mosher's suggested corrections submitted in writing in advance of the meeting.

5. CURRENT BUSINESS

A. <u>Audit Entrance Conference</u>

Finance Director Matusiewicz noted that staff has met with the auditors to discuss major transactions for the year. He further noted that this agenda item provides Finance Committee members the opportunity to get a brief introduction from the auditor on the audit planning process and to ask questions.

Mr. Patel spoke about auditor responsibilities in performance of the audit, the most important of which is to form and express an opinion on the financial statement. The audit is performed in accordance with governmental and generally accepted audit standards and is designed to give reasonable assurance that the financial statement is fairly presented in accordance with generally accepted accounting principles. When performing fieldwork the auditors will consider the internal control structure and at the conclusion of the audit will communicate in writing any significant matters. Mr. Patel indicated that his initial meeting with staff covered significant financial transactions, management operations and changes, and forthcoming pronouncements that are applicable for the current year. The most significant pronouncements include Statement 63 - Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position; and Statement 65 - Items Previously Reported as Assets and Liabilities.

In response to Council Member Petros' request, Mr. Patel further explained Statement 63. He noted that the government-wide financial statement will now show five elements that include assets; deferred outflow of resources, which is similar to prepay; liabilities; deferred inflow of resources, which is similar to unearned revenue; and net position.

Mr. Mosher commented that the audit process seems to be backward to what the City Charter specifies, namely that the City will retain the auditor at the beginning of the fiscal year instead of at the end of the year. Mr. Mosher questioned whether the audit will reveal incidents of embezzlement or other such behavior. Mr. Patel explained that the audit is not designed specifically for detecting such behavior; however, transactions are tested on a randomized basis and any findings would be reported to the Committee. He added that under the current standards, auditors are required to identify fraud in the financial statement audit and review internal control structure and segregation of duties in order to make such an identification. Council Member Henn noted this is all in accordance with standard practice for conducting an audit.

B. <u>City Insurance Renewals</u>

Mr. Matusiewicz stated the City Council will consider approval on renewal of the City's insurance policies at their June 25, 2013 meeting. This agenda item provides Finance Committee members the opportunity to ask questions on the premiums being charged for next year's coverage.

Mayor Curry questioned why there are significant increases in the premiums. Risk Manager Farley addressed the property insurance increase and noted that the addition of the Civic Center complex increased the total insured value 53% along with other property valuation assessments which gave a premium increase of about $320,000.

In discussing the excess general liability insurance premium, Ms. Farley explained that for about the past 15 years the City has been able to maintain a $500,000 self-insured retention (SIR) which is uncommonly low for a coastal, full-service city. Due to experiencing some recent losses and claims paid in excess of the $500,000 SIR limit, the quote from the current insurance carriers has a higher SIR of

$1 million. This was outlined as Option #1. Option #2 is a second tentative quote with a $500,000 SIR received from the CSAC Excess Insurance Authority. A decision at an underwriters meeting on Tuesday is pending to determine whether Big Canyon Reservoir will be included in the coverage since it is designated as a dam. Ms. Farley said if the outcome of the underwriters' decision is to exclude the reservoir, staff would recommend Option #1 to the City Council.

Ms. Farley explained the increase in the workers' comp insurance premium is due to the fact that medical expenses continue to escalate and there have been some significant claims that resulted in disability retirements.

In response to a question raised by Council Member Henn, Ms. Farley clarified that the deductible for earthquake and flood insurance is 10% of the insured value of the asset.

Mr. Mosher commented that the public would benefit from knowing what claims have been paid and he questioned whether the $50 million limit in excess general liability is sufficient. Ms. Farley reported that the City raised the general liability limit to $50 million based on a jury award of $50 million for a Dana Point bicycling claim. She stated the level is prudent and there is no cause to increase it to a higher limit based on actuarial review and comparison to benchmarking cities. She added that in the property insurance limit the City is in the upper band relative to benchmarked cities. There is no recommendation at this time to increase the limit.

Mr. Cassidy referred to the old City Hall and questioned whether it would be useful to have an account for discontinued assets. He asked what mechanism is used to track major variances to the budget. Mr. Matusiewicz noted he would report any major changes in the financial status as they occur to the Finance Committee. City Manager Kiff added the Quarterly Financial Report is another tool used to communicate financial status. Mr. Kiff stated that staff budgets revenues and expenditures in a conservative manner. This is a prudent practice and can result in having extra funds to report to Council at the end of the year.

It was suggested that next year it may be helpful to schedule a Finance Committee meeting with the insurance actuaries in January at the beginning of the application process and in advance of when the policies are up for review.

On a final note, Ms. Farley pointed out that if the Big Canyon Reservoir is approved by the CSAC underwriters committee, staff will prepare a Resolution for Council approval and bring it to the June 25, 2013 meeting.

C. <u>Fire Fee Schedule</u>

Mr. Matusiewicz introduced the item with an explanation of the cost study review of Fire Department fees that was prepared by MGT in conjunction with staff from the Fire and Finance Departments. An in-depth and comprehensive look at all the fees was completed resulting in major changes to planning and development fees, and the addition of new fees representing best practice industry standards. The inclusion of these new fees is consistent with the fees applied by a majority of Orange County cities and is closest to the model of Orange County Fire Authority. He noted the paramedic subscription fee, which had not been adjusted for 10 years, is proposed to increase from $48 a year to $60 a year.

In response to a question raised by Mayor Curry, Deputy Chief Kitch stated that new fees for service included in the proposed fee schedule are better aligned with the costs of performing the service. Chief Kitch explained the fees are broken into two components to cover planning and development for issuance on project approvals and inspection services for ongoing required annual maintenance. He noted that planning and development fees are reflective of the Fire Authority fee schedule which the building industry developers are familiar and comfortable with in Orange County. He commented the proposed fees are more fair and equitable because the fee is more representative of the service time it takes to provide the service. Mayor Curry expressed concern about adding new fees and said the staff report needs to better explain the new fees relative to what the fee structure was previously and answer how much more or less it will cost for a given service.

Council Member Henn agreed the fees have been expanded so much it may not be possible to show a breakdown comparison of the amount of revenue collected in the old categories against the expanded new categories. It was suggested to identify how the proposed fees stack up against Fire Authority fees and to have a representative of the building industry speak in support of the new fee structure. This would likely help people understand the new fee structure. Mr. Kiff suggested showing what the cost would be using the new fee schedule as a comparison on some actual projects that were done over the past year.

Council Member Petros stated if this is considered an impacting subject to the Government Code 66000 provisions, it should be demonstrated how these fees go up against the five findings in the Government Code section. He indicated that he wants to see how the fees were derived and he directed the structure be simplified if possible.

Council Member Henn commented that he would like to see a report at the end of fiscal year 2014 that will show a comparison of the aggregate difference in the fees collected, with an adjustment for volume, in the new structure compared to the old fee structure.

Mr. Matusiewicz spoke about the Junior Lifeguard fees and pointed out an error on the schedule for resident participants which lists the fee as $697 but should be $725 which is a 15% subsidy. Assistant Chief Williams said the current fee is $695 and the fee increase captures this year's CPI because as the fees were still being studied there was not a CPI increase. There was discussion about the resident fee increase and the amount of the subsidy. Council Member Petros questioned whether a higher subsidy should be considered given that the program is so popular and teaches children about ocean safety. Mayor Curry suggested raising the fee to $700 and increasing the amount of the subsidy percentage.

Mr. Matusiewicz went on to address fees for Emergency Medical Services that are currently subsidized at 80% and elimination of the subsidy is proposed to achieve full cost recovery. EMS Manager Ord explained the difference between Advanced Support and Basic Life Support (ALS and BLS) and the billing that occurs when a patient is transported by the paramedics or by ambulance. The Fire Medics program is voluntary for Newport Beach residents and she stated Fire Medics members would have no out of pocket costs for transports. Chief Poster gave further details about the analysis of the costs and noted the Orange County fee approved by the Board of Supervisors is higher than the City’s costs. He said the proposed fees are 1) completely justifiable given the City’s actual costs, 2) more simply structured, and 3) less than what the County charges. Council Member Henn stated the staff report should spell out those comparisons. There was further discussion about the subsidy and Council Member Henn asked for better clarity in the staff report. Mayor Curry said that staff should demonstrate how the fees are based on the results of the study, how the proposed fees compare to the fees of the County and neighboring cities, how insurance or the lack thereof impacts cost recovery, and how the subsidy works and is applied.

Mayor Curry noted this proposed fee schedule revision should be brought to the City Council at a Study Session prior to placing it on an agenda for adoption.

Mr. Mosher suggested it would be helpful to know what fraction of Fire Department activity is covered by property taxes and how much is not funded. He asked if he would be billed for a fire at his house and does it matter whether he called or somebody else reported the fire, and how aggressive is the City about collecting payment if he did get a bill and whether the Council thinks the City should be aggressive about that. He questioned whether the proposed fees will change as a result of the study by the consultant hired by Council to review the Fire Department and services. Council Member Henn commented that every department’s fees are studied on a 3-year cycle and the impact of any strategic changes in the fire service will be reflected in a future fee schedule update.

D. <u>Third Review of Facilities Financial Planning Tool (FFPT)</u>

Mr. Matusiewicz explained minor revisions made to the FFPT are the result of recent year-end budget action. He pointed out the average General Fund contribution over a 30-year period amounts to $10.6 million. Mr. Matusiewicz proposed bringing the FFPT to a City Council Study Session for review, if Finance Committee members are in agreement with the current iteration of the FFPT.

Council Member Henn questioned the timing for branch library projects. Mr. Kiff commented that community use of libraries is changing and it would be beneficial to wait a few years to include planning for rebuilding branch libraries after determining future usage of libraries. Mayor Curry and Council Member Henn were in agreement that the libraries should be reflected in the plan after 2024.

Council Member Henn noted it is important to show these important points in the staff report: include development fee contributions as a key planning highlight; note this iteration does not fully represent the potential for surplus asset disposition or monetization; and point out that although there is $20 million borrowing represented in the out years associated with rebuilding the Police headquarters, it is entirely possible that the plan will be cash funded and no borrowing will be needed.

Mr. Cassidy affirmed it is important to reflect all revenue such as for reuse of the old City Hall property and he spoke in support of the decision to build the Civic Center. Council Member Henn pointed out there is a line item for City Hall reuse represented. He agreed that there is some other revenue that isn't reflected but the key issue to convey is the money that was borrowed for building the Civic Center may well be the only borrowing associated with a 30-year plan to completely redo all of the City's key facilities.

E. Demonstration of Long-Range Fiscal Forecasting Tool

Deputy Director Montano demonstrated the MuniCast forecast trend analysis model which is used as an analytical tool to create baselines and alternative annual forecast of revenues and expenditures. He stated only General Fund is currently loaded in the model but it can also be used for Enterprise Funds. The goal is to further refine the model during the budget year for use in the decision making process.

Using the 32 revenue and 29 expenditure categories in the General Fund, Mr. Montano showed how the baseline assumptions can be adjusted +/- 5% to change the forecast picture. He also demonstrated how the interactive scenario assumptions can be used to reflect sensitivity analysis and estimate potential impacts of budget decisions moving forward.

Council Member Henn acknowledged use of this tool will be helpful in starting the financial planning cycle with the development of a strategic plan followed by developing the budget. Mr. Matusiewicz welcomed input on categories to include in the model that will help with making better informed decisions.

6. FINANCE COMMITTEE ANNOUNCEMENTS OR MATTERS WHICH MEMBERS WOULD LIKE PLACED ON A FUTURE AGENDA FOR DISCUSSION, ACTION OR REPORT (NON-DISCUSSION ITEM)

No future agenda items were discussed.

7. ADJOURNMENT

The Finance Committee adjourned at 6:00 p.m.

Filed with these minutes are copies of all material distributed at the meeting.

Attest:

______________________________ ______________________________

Mike Henn, Chair
Finance Committee Chair

Date

CITY OF NEWPORT BEACH
FINANCE COMMITTEE STAFF REPORT

July 22, 2013

TO: HONORABLE CHAIR AND MEMBERS OF THE COMMITTEE

FROM: Finance Department
Dan Matusiewicz, Finance Director
(949) 644-3123 or danm@newportbeachca.gov

SUBJECT: ANNUAL INVESTMENT POLICY REVIEW AND UPDATE

ABSTRACT:

Consistent with Section K-2 of Council Policy F-1, Statement of Investment Policy (the Policy), the Finance Department has completed an annual review of the Policy. The proposed changes better align the policy with California Government Code, allow for more flexibility to achieve an effective return through diversification, and provide greater clarity to the advisors while still achieving the paramount objectives of safety and liquidity. With Finance Committee concurrence, Finance staff will bring the suggested revisions to Council for formal approval. These changes do not materially affect, and are in furtherance of, the City's investment objectives. The recommendations do include changes to the maximum credit concentration, credit quality and allowable investments to provide more flexibility to diversify investments across asset classes.

BACKGROUND:

Pursuant to California Government Code Section 53600.5, when investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, the primary objective of the City Treasurer shall be to safeguard the principal of the funds under his/her control. The secondary objective shall be to meet the liquidity needs of the depositor. The third objective shall be to achieve a return on the funds under his/her control. The City's universe of available investments is limited by California law, and further limited to those types of securities the City deems appropriate in relation to its fiduciary duties of safety. Approximately 51% of the Medium-Term Investment Portfolio (MTIP) consists of agency securities, which are bonds and notes issued by government-sponsored enterprises, or GSEs, including Fannie Mae, Freddie Mac and the Federal Home Loan Bank. They are the highest-quality debt instruments after Federal Treasury securities, which make up approximately 23% of the City's MTIP.

Finance staff recently met with representatives from each of the City's financial investment advisory firms to solicit suggested changes to the Investment Policy. There is consensus among the advisors that suitable investment opportunities in agency securities and other investment grade securites are diminishing. This is largely due to the Federal Government's anticipated orderly transition of the mortgage market to private capital through a winding down of Fannie Mae and Freddie Mac and Federal Agency obligations becoming more expensive due to a shrinking supply. The proposed changes, described in detail below, better align the policy with State Code and provide greater clarity to the advisors. The proposed changes also allow for greater flexibility to diversify the City's investment portfolio to the extent permissible by State Code. In consultation with the City's investment advisors, Finance Staff recommends these changes to receive the highest rate of return reasonably available while also taking into account the primary goals of achieving safety and liquidity.

Below is a summary of the suggested changes by policy section. A comparison of these changes with what is allowable according to State Code is summarized in Attachment B.

Section C.3. Delegation of Authority – Finance staff proposes that the policy explicitly require the City's investment advisors be registered under the Investment Advisors Act of 1940 as promulgated by the Securities and Exchange Commission.

Section F. Safekeeping and Custody of Assets – Finance staff proposes to eliminate the reference to the physical delivery of securities since the City's bank custodian now only keeps electronic records of security certificates on the City's behalf.

Section G. Authorized Investments – Finance staff proposes to add language that in the event that an apparent discrepancy is found between this Policy and the Government Code, the more restrictive parameter(s) will take precedence. Additional proposed changes are as follows:

Proposed Change	Explanation
Section G.1.a: Proposed language explicitly states no limits to percentage invested in US treasury bills.	Provides greater clarity
Section G.1.b: Proposed language explicitly states no limits to the percentage of the portfolio that can be invested in federal instrumentality investments.	Provides greater clarity.
Section G.1.c: Proposed language explicitly states no limits to the percentage of the portfolio that can be invested in this category. Also re-categorizes and strikes certain language from G.1.c relating to mortgage backed securities and debentures to section G.1.d.	Provides greater clarity.
Section G.1.d: Consistent with State Code, the proposed change explicitly allows investment in collateralized mortgage obligation (CMOs).	Provides greater clarity

Proposed Change	**Explanation**
Section G.1.e: Proposed language extends maturities of medium term notes from four to five years and strikes authorization of AAA rated FDIC guaranteed corporate bonds due to expiration of Total Liqudity Guarantee Program (TLGP).	Provides for more flexibility to achieve greater investment diversification and opportunity. Deletes reference to expired TLGP program.
Section G.1.f: Proposed change allows for investment of notes or bonds of any of the 50 states, and increases limit from 15% to 30% of portfolio allowed to be invested in this category. Also allows for a minimum credit exposure of A as opposed to AA.	Provides for more flexibility to achieve greater diversification and investment opportunity. This change is allowed under State Code and provides better alignment with the policy constraints on a corporate medium-term note.
Section G.1.h: Proposed change provides authorization to invest negotiable certificates of deposit in federally or state licensed foreign savings institutions with senior long-term debt rated at least A or short-term debt rated at least A-1.	Change is allowed under state code and provides for more flexibility to achieve greater diversification and investment opportunity.
Section G.1.i: Proposed additional language to clarify acceptable rating of A-1 or equivalent for prime commercial paper investments.	Specificity adds greater clarity for advisors.
Section G.1.j: Proposed increase to the maximum allocation in bankers' acceptances from 20% to 40% of the City's total portfolio.	Changes are permissible by state code and allow for more flexibility to achieve greater diversification and investment opportunity.
Section G.1.n: Proposed change allows up to 10% (maximum allowable by law) of total portfolio be invested in any individual money market fund.	Changes are permissible by state code and allow for more flexibility to achieve greater diversification and liquidity.

Section H. Investment Parameters

Proposed Change	**Explanation**
Section 1: Proposed change in diversification language more clearly specifies the types of issues that are excepted from the 5% portfolio exposure limitation. These exceptions include: governmental issuers, investment pools, and money market funds.	Makes language consistent with state code and provides greater clarity.
Section 2: Proposed change more clearly specifies that advisors will monitor their own portfolios and not that of the other investment advisors.	Specificity adds greater clarity for advisors.

Proposed Change	Explanation
Section 3: Proposed change allows for less than three quotes for competitive transactions when it is not possible to obtain three quotes.	Specificity adds greater clarity for advisors when three quotes are not obtainable.

Section I. Portfolio Performance – Historically the City has evaluated portfolio performance against the Bank of America Merrill Lynch (BAML) 1-3 Treasury Index. Since the BAML 1-3 Treasury Index does not include agencies or corporate securities, staff is considering an alternative benchmark that more closely resembles the City's current investment mix. Therefore, staff recommends revising the policy to include language that allows for using comparative benchmark indexes that more closely correspond to the portfolio's duration, universe of allowable securities, risk profile, and other relevant characteristics. These indexes will be used as reference points to assess the performance of the City's investment portfolio. Based on the composition of the available alternatives, staff believes the Bank of America Merrill Lynch (BAML) 1-3 Year AAA-A Corporate and Government Index (Bloomberg index number "B110") is more generally representative of our medium turn portfolio. Staff also recommends the use of a short-term performance benchmark such as the BAML 91 day Treasury Index and the BAML 0-1 Year Treasury index to assess the performance of the City's short-term portfolio.

Section J. Reporting – Finance staff proposes additional language that requires the inclusion of investment buy/sell transactions to the monthly treasury report. This will provide a greater level of transparency.

CONCLUSION:

For purposes of ensuring consistency with the overall objectives of preservation of principal, liquidity and return, and its relevance to current law and financial and economic trends, staff is proposing changes to Council Policy F-1, Statement of Investment Policy. These changes do not materially affect investment objectives. The recommendations do include changes to the maximum credit concentration, credit quality and allowable investments to provide more flexibility to diversify investments across asset classes. With Finance Committee concurrence, Finance staff will bring the suggested revisions to Council for formal approval.

Prepared by:	Submitted by:
/s/Steve Montano	/s/Dan Matusiewicz
Steve Montano	Dan Matusiewicz
Deputy Finance Director	Finance Director

Attachments:
A. Redline Investment Policy Amendment
B. CA Gov. Code & Proposed Changes to Authorized Investments

STATEMENT OF INVESTMENT POLICY

PURPOSE:
The City Council has adopted this Investment Policy (the Policy) in order to establish the scope of the investment policy, investment objectives, standards of care, authorized investments, investment parameters, reporting, investment policy compliance and adoption, and the safekeeping and custody of assets.

This Policy is organized in the following sections:

A. Scope of Investment Policy
   1. Pooling of Funds
   2. Funds Included in the Policy
   3. Funds Excluded from the Policy
B. Investment Objectives
   1. Safety
   2. Liquidity
   3. Yield
C. Standards of Care
   1. Prudence
   2. Ethics and Conflicts of Interest
   3. Delegation of Authority
   4. Internal Controls
D. Banking Services
E. Broker/Dealers
F. Safekeeping and Custody of Assets
G. Authorized Investments
   1. Investments Specifically Permitted
   2. Investments Specifically Not Permitted
   3. Exceptions to Prohibited and Restricted Investments
H. Investment Parameters
   1. Diversification
   2. Maximum Maturities
   3. Credit Quality
   4. Competitive Transactions
I. Portfolio Performance
J. Reporting
K. Investment Policy Compliance and Adoption
   1. Compliance
   2. Adoption

A. SCOPE OF INVESTMENT POLICY

1. Pooling of Funds

All cash shall be pooled for investment purposes. The investment income derived from the pooled investment shall be allocated to the contributing funds, net of all banking and investing expenses, based upon the proportion of the respective average balances relative to the total pooled balance. Investment income shall be distributed to the individual funds not less than annually.

2. Funds Included in the Policy

The provisions of this Policy shall apply to all financial assets of the City as accounted for in the City's Comprehensive Annual Financial Report, including;

a) General Fund
b) Special Revenue Funds
c) Capital Project Funds
d) Enterprise Funds
e) Internal Service Funds
f) Trust and Agency Funds
g) Permanent Endowment Funds
h) Any new fund created unless specifically exempted

If the City invests funds on behalf of another agency and, if that agency does not have its own investment policy, this Policy shall govern the agency's investments.

3. Funds Excluded from this Policy

Bond Proceeds – Investment of bond proceeds will be made in accordance with applicable bond indentures.

B. INVESTMENT OBJECTIVES

The City's funds shall be invested in accordance with all applicable City 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. Safety

Preservation 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 objective shall be to mitigate credit risk and interest rate risk. To attain this objective, the City shall diversify its investments by investing funds among several financial institutions and a variety of securities offering independent returns.

a) <u>Credit Risk</u>
The City shall minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

- Limiting investments in securities that have higher credit risks, pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisors with which the City will do business
- Diversifying the investment portfolio so as to minimize the impact any one industry/investment class can have on the portfolio

b) <u>Interest Rate Risk</u>
To minimize the negative impact of material changes in the market value of securities in the portfolio, the City shall:

- Structure the investment portfolio so that securities mature concurrent with cash needs to meet anticipated demands, thereby avoiding the need to sell securities on the open market prior to maturity
- Invest in securities of varying maturities

2. Liquidity
The City's investment portfolio shall remain sufficiently liquid to enable the City to meet all operating requirements which might be reasonably anticipated without requiring a sale of securities. Since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets. A portion of the portfolio also may be placed in money market mutual funds or LAIF which offer same-day liquidity for short-term funds.

3. Yield
The City's investment portfolio shall be designed with the objective of attaining a benchmark rate of return throughout budgetary and economic cycles, commensurate with the City's investment risk constraints and the liquidity characteristics of the portfolio. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core of investments is limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed.

C. STANDARDS OF CARE

1. Prudence

The standard of prudence to be used for managing the City's investment program is California Government Code Section 53600.3, the prudent investor standard, which states that "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 City's overall investment program shall be designed and managed with a degree of professionalism that is worthy of the public trust. The City recognizes that no investment is totally without risk and that the investment activities of the City are a matter of public record. Accordingly, the City 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 City.

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

2. Ethics and Conflicts of Interest

Elected officials and employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution of the City's investment program or could impair or create the appearance of an impairment of their ability to make impartial investment decisions. Employees and investment officials shall subordinate their personal investment transactions to those of the City. In addition, City Council members, the City Manager, and the Finance Director shall file a Statement of Economic Interests each year as required by California

Government Code Section 87203 and regulations of the Fair Political Practices Commission.

3. Delegation of Authority

Authority to manage the City's investment program is derived from the Charter of the City of Newport Beach section 605 (j). The Finance Director shall assume the title of and act as City Treasurer and with the approval of the City Manager appoint deputies annually as necessary to act under the provisions of any law requiring or permitting action by the City Treasurer. The Finance Director may then delegate the authority to conduct investment transactions and to manage the operation of the investment portfolio to other specifically authorized staff members. No person may engage in an investment transaction except as expressly provided under the terms of this Policy.

The City may engage the support services of outside investment advisors with respect 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 City's financial resources. Such companies must be registered under the Investment Advisors Act of 1940, be well-established and exceptionally reputable. Members of the staff of such companies who will have primary responsibility for managing the City's investments must have a working familiarity with the special requirements and constraints of investing municipal funds in general and this City's funds in particular. These firms must insure that the portion of the portfolio under their management complies with various concentration and other constraints specified herein, and contractually agree to conform to all provisions of governing law and the collateralization and other requirements of this Policy. Selection and retention of broker/dealers by investment advisors shall be at their sole discretion and dependent upon selection and retention criteria as stated in the Uniform Application for Investment Advisor Registration and related Amendments (SEC Form ADV 2A).

4. Internal Controls

The Finance Director is responsible for establishing and maintaining a system of internal controls. The internal controls shall be designed to prevent losses of public funds arising from fraud, employee error, and misrepresentation by third parties, unanticipated changes in financial markets, or imprudent action by City employees and officers. The internal structure shall be designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived, and (2) the valuation of costs and benefits requires estimates and judgments by management.

D. BANKING SERVICES

Banking services for the City shall be provided by FDIC insured banks approved to provide depository and other banking services. To be eligible, a bank shall 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 insurance coverage in accordance with California Government Code Section 53652.

E. BROKER/DEALERS

In the event that an investment advisor is not used to purchase securities, the City will select broker/dealers on the basis of their expertise in public cash management and their ability to provide service to the City’s account.

Each approved broker/dealer must possess an authorizing certificate from the California Commissioner of Corporations as required by Section 25210 of the California Corporations Code.

To be eligible, a firm must meet at least one of the following criteria:

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

F. SAFEKEEPING AND CUSTODY OF ASSETS

The Finance Director shall select one or more banks to provide safekeeping and custodial services for the City. A Safekeeping Agreement approved by the City 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 City'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 City. Sufficient evidence to title shall be consistent with modern investment, banking and commercial practices.

All investment securities, except non-negotiable Certificates of Deposit, Money Market Funds and local government investment pools, purchased by the City will be delivered by ~~either~~ book entry ~~or physical delivery~~ and will be held in third-party safekeeping by a City approved custodian bank, its correspondent bank or its Depository Trust Company (DTC) participant account.

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

G. AUTHORIZED INVESTMENTS

All investments and deposits of the City shall be made in accordance with California Government Code Sections 16429.1, 53600-53609 and 53630-53686. Any revisions or extensions of these code sections will be assumed to be part of this Policy immediately upon being enacted. The City has further restricted the eligible types of securities and transactions. The foregoing list of authorized securities and transactions shall be strictly interpreted. Any deviation from this list must be pre-approved by resolution of the City Council. In the event an apparent discrepancy is found between this Policy and the Government Code, the more restrictive parameter(s) will take precedence.

1. Investments Specifically Permitted

   a) United States Treasury bills, notes, or bonds with a final maturity not exceeding five years from the date of trade settlement. There is no limitation as to the percentage of the City's portfolio that may be invested in this category.

   b) Federal Instrumentality (government-sponsored enterprise) debentures, discount notes, callable and step-up securities, with a final maturity not exceeding five years from the date of trade settlement. There is no limitation as to the percentage of the portfolio that can be invested in this category.

c) 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 ~~mortgage-backed securities and debentures with a final maturity not exceeding five years from the date of trade settlement.~~final maturity not exceeding five years from the date of trade settlement. There is no limitation as to the percentage of the portfolio that can be invested in this category.

d) Mortgage-backed Securities, Collateralized Mortgage Obligation (CMO) and Asset-backed Securities limited to mortgage-backed pass-through securities issued by a US government agency, or consumer receivable pass-through certificates or bonds with a final maturity not exceeding five years from the date of trade settlement. Securities eligible for investment under this subdivision shall be issued by an issuer whose debt is rated at least "A" or the equivalent by a Nationally Recognized Statistical Rating Organization (NRSRO). The security itself shall be rated at least "AAA" or the equivalent by an NRSRO. No more than five percent (5%) of the City's total portfolio shall be invested in any one issuer of mortgage-backed and asset-backed securities listed above, and the aggregate investment in mortgage-backed and asset-backed securities shall not exceed twenty percent (20%) of the City's total portfolio.

e) 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 ~~four~~ five years from the date of trade settlement, and rated at least A or the equivalent by an NRSRO. No more than five percent (5%) of the City's total portfolio shall be invested in any one issuer of medium-term notes, and the aggregate investment in medium-term notes shall not exceed thirty percent (30%) of the City's total portfolio. ~~In addition, AAA rated FDIC-guaranteed corporate bonds are herein authorized, within the aforementioned diversification and maturity requirements.~~

f) Municipal Bonds~~: General and Revenue obligations of the State of California and local agencies within the State. Municipal bonds must be rated at least AA by two NRSROs with maturities not exceeding three years. No more than five percent (5%) of the City's total portfolio shall be invested in any one issuer and the aggregate investment in municipal bonds shall not exceed fifteen percent (15%) of the City's total portfolio.~~ 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. Investments of local agencies not at State treasury level are not permitted.

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, or operated by the local agency, or by a department, board, agency, or authority of the local agency are permitted.

Municipal bonds must be rated at least "A" or the equivalent by an NRSRO with maturities not exceeding five years from the date of trade settlement. No more than five percent (5%) of the City'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 thirty percent (30%) of the portfolio.

g) Non-negotiable Certificates of Deposit and savings deposits with a maturity not exceeding two years from the date of trade settlement, in FDIC insured state or nationally chartered banks or savings banks that qualify as a depository of public funds in the State of California as defined in California Government Code Section 53630.5. Deposits exceeding the FDIC insured amount shall be secured pursuant to California Government Code Section 53652. No one issuer shall exceed more than five percent (5%) of the portfolio, and investment in negotiable and nonnegotiable certificates of deposit shall be limited to thirty percent (30%) of the portfolio combined.

h) Negotiable Certificates of Deposit only with 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 federally licensed or state-licensed branch of a foreign bank ~~U.S. Banks~~ whose senior long-term debt is rated at least "A", or the equivalent, or short-term debt is rated at least "A-1"~~underlying securities are rated A-1~~ or the equivalent by an NRSRO and having assets in excess of $10 billion, so as to insure security and a large, well-established secondary market. Ease of subsequent marketability is further ascertained prior to initial investment by examining currently quoted bids by primary dealers and the acceptability of the issuer by these dealers. No one issuer shall exceed more than five percent (5%) of the portfolio, and maturity shall not exceed two years. Investment in negotiable and non-negotiable ~~-~~certificates of deposit shall be limited to thirty percent (30%) of the portfolio combined.

i) Prime Commercial Paper with a maturity not exceeding 270 days from the date of trade settlement that are rated "A-1", or the equivalent, ~~with the highest letter and number rating as provided for~~ by an NRSRO. The entity that issues the commercial paper shall meet all of the following conditions in either sub-paragraph i. or sub-paragraph ii. below:

i. The entity shall (1) be organized and operating in the United States as a general corporation, (2) have total assets in excess of $500,000,000 and (3) have debt other than commercial paper, if any, that is rated at least "A" or the equivalent by an NRSRO.

ii. 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 at least "A-1" or the equivalent~~,~~ by an NRSRO.

iii. No more than five percent (5%) of the City's total portfolio shall be invested in the commercial paper of any one issuer, and the aggregate investment in commercial paper shall not exceed twenty five percent (25%) of the City's total portfolio.

j) Eligible Banker's Acceptances with a maturity not exceeding 180 days from the date of trade settlement, drawn on and accepted by a commercial bank whose senior long-term debt is rated at least "A" or the equivalent by an NRSRO at the time of purchase. Banker's Acceptances shall be rated at least "A-1", ~~P-1~~ or the equivalent at the time of purchase by an NRSRO. If the bank has senior debt outstanding, it must be rated at least "A" or the equivalent by an NRSRO. The aggregate investment in banker's acceptances shall not exceed ~~twenty~~ forty percent (~~2~~40%) of the City's total portfolio, and no more than five percent (5%) of the City's total portfolio shall be invested in banker's acceptances of any one bank.

k) Repurchase Agreements and Reverse Repurchase Agreements with a final termination date not exceeding 30 days collateralized by U.S. Treasury obligations or Federal Instrumentality securities listed in items 1 and 2 above with the maturity of the collateral not exceeding ten years. For the purpose of this section, the term collateral shall mean purchased securities under the terms of the City's approved Master Repurchase Agreement. The purchased securities shall have a minimum market value including accrued interest of one hundred and two percent (102%) of the dollar value of the funds borrowed. Collateral shall be held in the City's custodian bank, as safekeeping agent, and the market value of the collateral securities shall be marked-to-the-market daily.

Repurchase Agreements and Reverse Repurchase Agreements shall be entered into only with broker/dealers and who are recognized as Primary Dealers with the Federal Reserve Bank of New York, or with firms that have a Primary Dealer within their holding company structure. Primary Dealers approved as Repurchase Agreement counterparties shall have a short-term credit rating of at least "A-1" or the equivalent and a long-term credit rating of at least "A" or the equivalent. Repurchase agreement counterparties shall execute a City approved Master Repurchase Agreement with the City. The Finance Director shall maintain a copy of the City's approved Master Repurchase Agreement and a list of the broker/dealers who have executed same.

In addition, the City must own assets for more than 30 days before they can be used as collateral for a reverse repurchase agreement.

No more than ten percent (10%) of the portfolio can be involved in reverse repurchase agreements.

l) State of California's Local Agency Investment Fund (LAIF), pursuant to California Government Code Section 16429.1.

m) County Investment Funds: Los Angeles County provides a service similar to LAIF for municipal and other government entities outside of Los Angeles County, including the City. Investment in this pool is intended to be used as a temporary repository for short-term funds used for liquidity purposes. The Finance Director shall maintain on file appropriate information concerning the county pool's current investment policies, practices, and performance, as well as its requirements for participation, including, but not limited to, limitations on deposits or withdrawals and the composition of the portfolio. At no time shall more than five percent (5%) of the City's total investment portfolio be placed in this pool.

n) 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 in the applicable California statutes and (4) have a rating of at least AAA or the equivalent by at least two NRSROs. The aggregate investment in money market funds shall not exceed twenty percent (20%) of the City's total portfolio and no more than ten percent (10%) of the City's total portfolio shall be invested in any one fund.

2. Investments Specifically Not Permitted

Any security type or structure not specifically approved by this policy is hereby prohibited. Security types, which are thereby prohibited include, but are not limited to: "exotic" derivative structures such as range notes, dual index notes, inverse floating rate notes, leveraged or de-leveraged floating rate notes, interest only strips that are derived from a pool of mortgages and any security that could result in zero interest accrual if held to maturity, or any other complex variable or structured note with an unusually high degree of volatility risk.

The City shall not invest funds with the Orange County Pool.

3. Exceptions to Prohibited and Restricted Investments

The City shall not be required to sell securities prohibited or restricted in this policy, or any future policies, or prohibited or restricted by new State regulations, if purchased prior to their prohibition and/or restriction. Insofar as these securities provided no notable credit risk to the City, holding of these securities until maturity is approved. At maturity or liquidation, such monies shall be reinvested as provided by this policy.

H. INVESTMENT PARAMETERS

1. Diversification

The City shall diversify its investments to avoid incurring unreasonable risks inherent in over-investing in specific instruments, individual financial institutions or maturities. As such, no more than five percent (5%) of the City's portfolio may be invested in the instruments of any one ~~non-governmental~~ issuer, except governmental issuers, investment pools and Money Market Funds. This restriction does not apply to any type of Federal Instrumentality or Federal Agency Security listed in Sections G1 b and G1 c above. Nevertheless, the asset allocation in the investment portfolio should be flexible depending upon the outlook for the economy, the securities markets and the City's anticipated cash flow needs.

2. Maximum Maturities

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

3. Credit Quality

The City shall not purchase any security rated "A1" and / or "A+" or below if that security has been placed on "credit watch" for a possible downgrade by an NRSRO.

Each investment manager will monitor the credit quality of the securities in their respective portfolio. In the event a security held by the City is the subject of a rating downgrade which brings it below accepted minimums specified herein, or the security is placed on negative credit watch, where downgrade could result in a rate drop below acceptable levels, the investment advisor who purchased the security will immediately notify the Finance Director. The City shall not be required to immediately sell such securities. The course of action to be followed will then be decided on a case by case basis, considering such factors as the reason for the rate drop, prognosis for recovery or further drop, and market price of the security. The City Council will be advised of the situation and intended course of action.

4. Competitive Transactions
Investment advisors shall make best effort to price investment transactions ~~—~~on a competitive basis with broker/dealers selected consistent with their practices disclosed in form ADV 2A filed with the SEC. Where possible, ~~A~~at least three broker/dealers shall be contacted for each transaction and their bid or offering prices shall be recorded. If there is no other readily available competitive offering, the investment advisor shall make their best efforts to document quotations for comparable or alternative securities. If qualitative characteristics of a transaction, including, but not limited to, complexity of the transaction, or sector expertise of the broker, prevent a competitive selection process, investment advisors shall use brokerage selection practices as described above.

I. 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 City's investments shall be compared to the total return of a benchmark that most closely corresponds to the portfolio's duration, universe of allowable securities, risk profile, and other relevant characteristics. ~~The performance of the City'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 City's portfolio, its rate of return will be computed consistent with Global Investment Performance Standards (GIPS).

J. REPORTING
Monthly, the Finance Director shall produce a treasury report of the investment portfolio balances, transactions, risk characteristics, earnings, and performance results of the City's investment portfolio available to City Council and the public on the City's Website. 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 City;
2. A description of the funds, investments and programs;

3. 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;
4. A statement of compliance with this Policy or an explanation for non-compliance

K. INVESTMENT POLICY COMPLIANCE AND ADOPTION

1. Compliance
Any deviation from the policy shall be reported to Finance Committee as soon as practical, but no later than the next scheduled Finance Committee meeting. Upon recommendation of the Finance Committee, the Finance Director shall review deviations from policy with the City Council.

2. Adoption
The Finance Director shall review the Investment Policy with the Finance Committee at least annually to ensure its consistency with the overall objectives of preservation of principal, liquidity and return, and its relevance to current law and financial and economic trends.

The Finance Director shall review the Investment Policy with City Council at a public meeting if there are changes recommended to the Investment Policy.

This Policy was endorsed and adopted by the City Council of the City of Newport Beach on October 9, 2012. It replaces any previous investment policy or investment procedures of the City.

Adopted – April 6, 1959
Amended – November 9, 1970
Amended – February 11, 1974
Amended – February 9, 1981
Amended – October 27, 1986
Rewritten – October 22, 1990
Amended – January 28, 1991
Amended – January 24, 1994
Amended – January 9, 1995
Amended – April 22, 1996
Corrected – January 27, 1997
Amended – February 24, 1997
Amended – May 26, 1998
Reaffirmed – March 22, 1999
Reaffirmed – March 14, 2000
Amended & Reaffirmed – May 8, 2001
Amended & Reaffirmed – April 23, 2002

Amended & Reaffirmed – April 8, 2003
Amended & Reaffirmed – April 13, 2004
Amended & Reaffirmed – September 13, 2005
Amended – August 11, 2009
Amended & Reaffirmed – August 10, 2010
Amended & Reaffirmed – September 28, 2010
Reaffirmed – June 28, 2011
Amended & Reaffirmed – October 9, 2012

City of Newport Beach
Attachment B
CA Gov. Code & Proposed Changes to Authorized Investments
July, 2013

NB Policy Ref.	INVESTMENT TYPE	CA GOV. CODE	CURRENT NEWPORT BEACH POLICY	PROPOSED CHANGES TO CNB POLICY
G.1. a)	U.S. TREASURY OBLIGATIONS	5 YEARS MAX MATURITY	5 YEARS MAX MATURITY	
		NO MAX % OF PORTFOLIO	NOT STATED	NO MAX % OF PORTFOLIO
		NO MAX % OF ONE ISSUER	NOT STATED	NO MAX % OF ONE ISSUER
b)	FEDERAL INSTRUMENTALITY	5 YEARS MAX MATURITY	5 YEARS MAX MATURITY	
		NO MAX % OF PORTFOLIO	NOT STATED	NO MAX % OF PORTFOLIO
		NO MAX % OF ONE ISSUER	NOT STATED	NO MAX % OF ONE ISSUER
c)	FEDERAL AGENCY OBLIGATIONS	5 YEARS MAX MATURITY	5 YEARS MAX MATURITY	
		NO MAX % OF PORTFOLIO	NOT STATED	NO MAX % OF PORTFOLIO
		NO MAX % OF ONE ISSUER	NOT STATED	NO MAX % OF ONE ISSUER
d)	MORTAGE PASS - THROUGH SECURITIES	5 YEARS MAX MATURITY	5 YEARS MAX MATURITY	Clarification that investments in collateralized mortgage obligation (CMOs) - permissible under Cal Gov Code Sect 53601 (o)
		20% MAX OF PORTFOLIO	20% MAX OF PORTFOLIO	
		NO MAX % OF ONE ISSUER	5% MAX ONE ISSUER	
		RATED AT LEAST AA	RATED AT LEAST AAA	
e)	MEDIUM - TERM NOTES	5 YEARS MAX MATURITY	4 YEARS MAX MATURITY	5 YEARS MAX MATURITY
		30% MAX OF PORTFOLIO	30% MAX OF PORTFOLIO	
		NO MAX % OF ONE ISSUER	5% MAX ONE ISSUER	
		RATED AT LEAST A	RATED AT LEAST A	
f)	LOCAL AGENCY BONDS	5 YEARS MAX MATURITY	3 YEARS MAX MATURITY	
		NO MAX % OF PORTFOLIO	15% MAX OF PORTFOLIO	30% MAX OF PORTFOLIO
		NO MAX % OF ONE ISSUER	5% MAX ONE ISSUER	ANY OF THE 50 STATES
		NO MIN CREDIT QUALITY	RATED AT LEAST AA	RATED AT LEAST A
g)	NON-NEGOTIABLE CERTIFICATES OF DEPOSIT	5 YEARS MAX MATURITY	2 YEARS MAX MATURITY	
		NO MAX % OF PORTFOLIO	30% MAX OF PORTFOLIO	
		NO MAX % OF ONE ISSUER	5% MAX ONE ISSUER	
h)	NEGOTIABLE CERTIFICATES OF DEPOSIT/CD PLACEMENT SERVICE	5 YEARS MAX MATURITY	2 YEARS MAX MATURITY	Authorization to invest in licensed foreign saving institutions w/ senior long-term debt rated at least A or short-term debt rated at least A-1 - permissible under Cal Gov Code Sect 53601 (i)
		30% MAX OF PORTFOLIO	30% MAX OF PORTFOLIO	
		NO MAX % OF ONE ISSUER	5% MAX ONE ISSUER	
		NO MIN CREDIT QUALITY	RATED AT LEAST A-1	
I)	PRIME COMMERCIAL PAPER	270 DAYS MAX MATURITY	270 DAYS MAX MATURITY	Clarifies acceptable rating of A-1 or equivalent for prime commercial paper investments.
		25% MAX OF PORTFOLIO	25% MAX OF PORTFOLIO	
		10% MAX ONE ISSUER	5% MAX ONE ISSUER	
		RATED AT LEAST A-1	RATED AT LEAST A-1	
J)	BANKERS' ACCEPTANCES	180 DAYS MAX MATURITY	180 DAYS MAX MATURITY	
		40% MAX OF PORTFOLIO	20% MAX OF PORTFOLIO	40% MAX OF PORTFOLIO
		30% MAX ONE ISSUER	5% MAX ONE ISSUER	
		NO MIN CREDIT QUALITY	RATED AT LEAST A-1	
k)	REPURCHASE AGREEMENTS	1 YEAR MAX MATURITY	30 DAYS MAX MATURITY	
		NO MAX % OF PORTFOLIO	NOT STATED	
		NO MAX % OF ONE ISSUER	NOT STATED	
		NO MIN CREDIT QUALITY	SHORT TERM AT LEAST A-1	
		NO MIN CREDIT QUALITY	LONG TERM AT LEAST A	
	REVERSE REPURCHASE AGREEMENTS	92 DAYS MAX MATURITY	30 DAYS MAX MATURITY	
		20% MAX OF PORTFOLIO	10% MAX OF PORTFOLIO	
		NO MAX % OF ONE ISSUER	NOT STATED	
		NO MIN CREDIT QUALITY	NOT STATED	
l)	LOCAL AGENCY INVESTMENT FUND (LAIF)	N/A	N/A	
		NO MAX % OF PORTFOLIO	NO MAX % OF PORTFOLIO	
		N/A	N/A	
m)	LA COUNTY POOLED INVESTMENT FUNDS	N/A	SHORT TERM	
		NO MAX % OF PORTFOLIO	5% MAX OF PORTFOLIO	
		N/A	N/A	
	OC COUNTY POOLED INVESTMENT FUNDS	N/A	N/A	
		NO MAX % OF PORTFOLIO	PROHIBITED	
		N/A	N/A	
n)	MUTUAL FUNDS AND MONEY MARKET MUTUAL FUNDS	N/A	N/A	
		20% MAX OF PORTFOLIO	20% MAX OF PORTFOLIO	
		10% MAX ONE ISSUER	NOT STATED	10% MAX ONE ISSUER
		RATED AAA	RATED AAA	

CITY OF NEWPORT BEACH
FINANCE COMMITTEE STAFF REPORT

July 22, 2013

TO: HONORABLE CHAIR AND MEMBERS OF THE COMMITTEE

FROM: Finance Department
Dan Matusiewicz, Finance Director
(949) 644-3123 or Danm@newportbeachca.gov

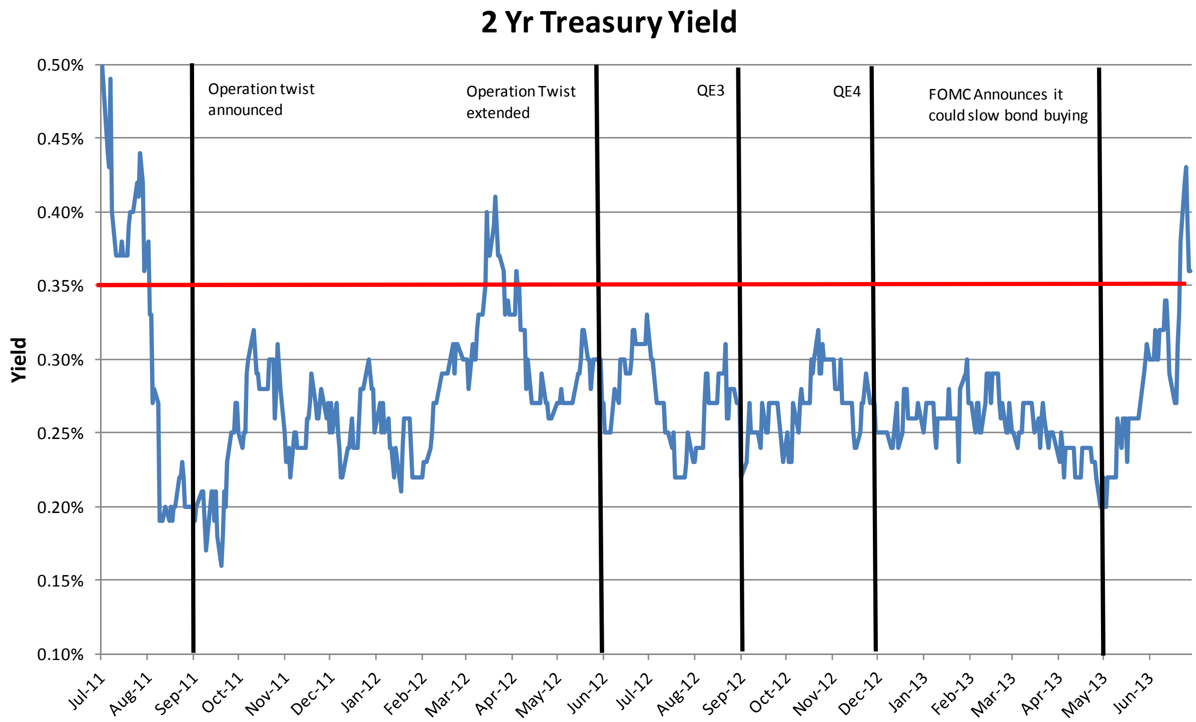
SUBJECT: ANNUAL INVESTMENT PORTFOLIO PERFORMANCE REVIEW

ABSTRACT:

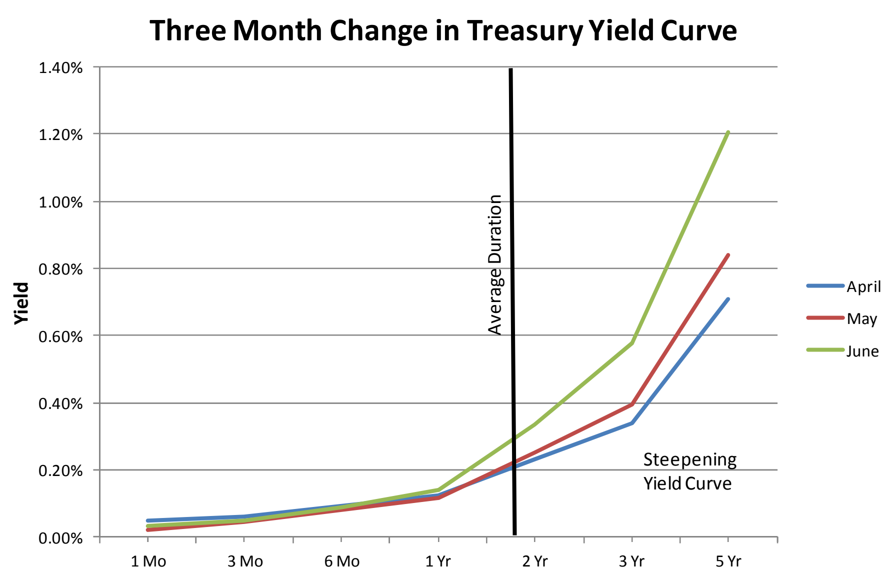
The purpose of this report is to summarize the performance of the City's investment portfolios relative to the City's investment objectives and pertinent performance benchmarks. With the prospect of long-term interest rates rising, investors have recently reacted by selling bonds and driving yields up. This caused fixed income portfolios to decline in value during May and June as interest rates rose across the yield curve. The City's medium-term portfolio annual average total return fell from 1.22% to 0.21% during the fiscal year, while the benchmark's total return fell from 1.06% to 0.66%. This is largely attributable to negative monthly returns in May and June of -0.27% and -0.35%, respectively, due to rapidly rising interest rates. While "total return" reflects the recent rapid change in market value, the portfolio's yield, if held to maturity, is currently .77% (at cost). If the rising interest environment is sustained, the prospect of higher future portfolio yields will return as new securities are purchased.

BOND MARKET OVERVIEW:

Throughout the fiscal year the yield on two year treasury notes has remained under 0.35%. The policy of the Federal Reserve (Fed) has been to keep short-term rates at record lows until unemployment reaches 6.5% and inflation is under 2.0%. In late April of 2013, officials predicted that unemployment will fall to 6.5% by the end of 2014, sooner than previous projections, and that inflation will run between 1.4% and 2.0% next year. Comments from Fed Chairman Ben Bernanke at a congressional hearing in May indicated the Fed could begin reducing bond purchases as early as September 2013.



With the prospect of long-term interest rates rising, investors reacted by selling bonds and driving yields up in recent months. This caused fixed income portfolios to decline in value during May and June as interest rates rose across the yield curve. Unrealized gains and losses are not realized unless securities are sold prior to maturity. However, they do have an immediate impact on the market value of the portfolio and total monthly return.



Not surprising, the City saw a decline in its medium-term portfolio for the first time in the past several years. These declines are short-term in nature and are consistent with the overall market move. This higher interest rate environment signifies that new investments should result in higher yields than the previous fiscal year.

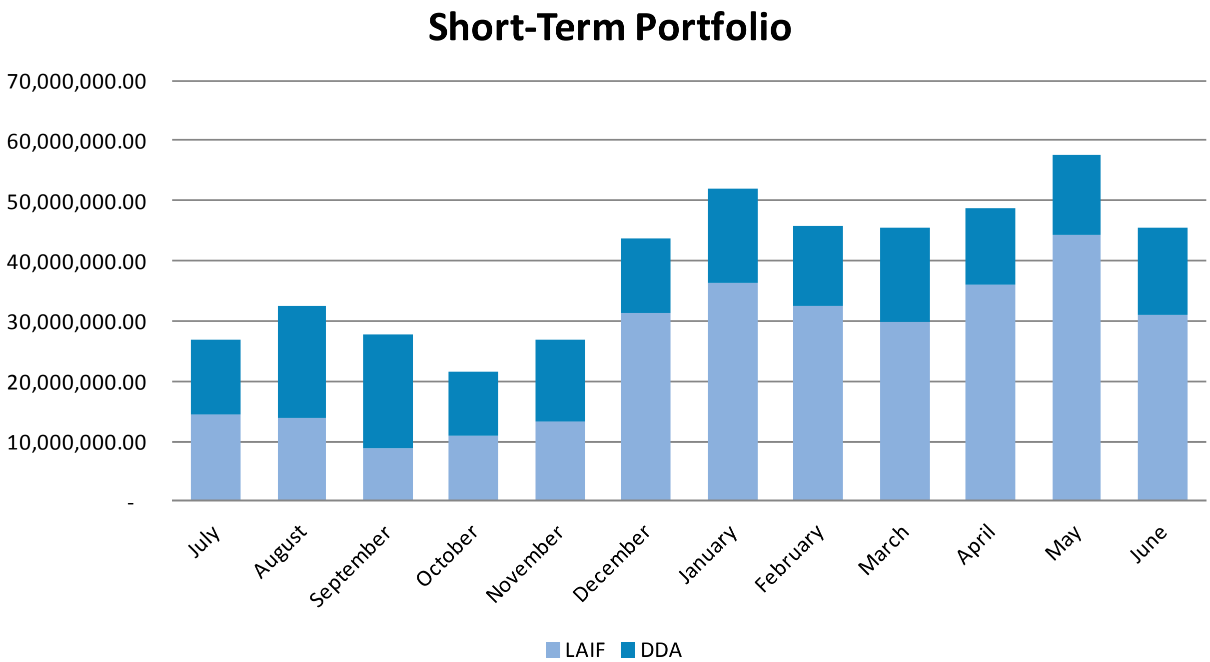
PORTFOLIO OVERVIEW:

Guided by Council Policy F-1 and constrained by state law, the City's core investment objectives are to provide safety of the invested principal by maintaining a well diversified, high quality portfolio of liquid assets while earning a market rate of return commensurate with the City's conservative risk profile. California State Code Section 53600.5 mandates that the City Treasurer shall follow three objectives when investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds. The primary objective of the City Treasurer shall be to safeguard the principal of the funds under its control. The secondary objective shall be to meet the liquidity needs of the City. The third objective shall be to achieve a return on the funds under his or her control.

Short-Term Portfolio

The City uses a combination of demand deposit accounts (DDA) and the Local Agency Investment Fund (LAIF) in its short-term portfolio to provide sufficient liquidity to meet its operating requirements. Per California Government Code section 16429.3, the State may not impound, seize, transfer or borrow funds in order to resolve their budget deficits. The average investment life of the LAIF fund is approximately 278 days. The average effective yield is 0.25%. Due to the low interest rate environment, larger DDA balances were maintained than usual due to attractive compensating balance credits utilized to offset banking costs.

The chart on the following page illustrates the LAIF and DDA balances maintained during the year.



Prior to the recent construction activities related to the Civic Center, the City's short-term investment portfolio averaged $20M. Over the past year it has increased to over $50M based on both current and anticipated liquidity needs related to the capital improvement projects identified in the Facilities Financing Planning Program.

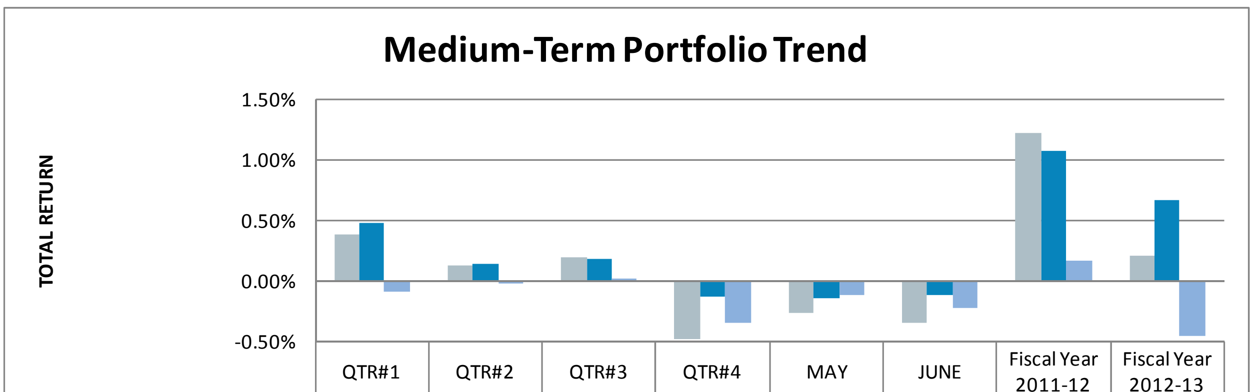
Medium-Term Portfolio

Funds that are unlikely to be spent in the foreseeable future are kept in a medium-term portfolio actively managed by three individual investment advisors in accordance with all applicable City policies and codes, State statutes, and Federal regulations. The City has proceeds from bonds are issued for a specific purpose and are governed by their own bond indentures.

The City's entire investment portfolio as of June 30, 2013 is summarized as follows:

Portfolios	June 30, 2013								
Operating Portfolios	Amortized Cost	Unrealized Gains/(Loss)	Fair Value	Accrued Interest	Market Value	% Total	YTM @ Cost	YTM @ Market	Notes
Short-term Portfolio									
Demand Deposit Accounts	$ 14,695,497	$ -	$ 14,695,497	$ -	$ 14,695,497	7.16%	0.54%	0.54%	(1)
Local Agency Investment Fund	30,901,523	-	30,901,523	-	30,901,523	15.06%	0.24%	0.24%	(2)
Medium-term Portfolio									
Cash Equivalents	3,642,967	-	3,642,967	-	3,642,967	1.78%	0.06%	0.06%	
Marketable Securities	155,565,300	(348,757)	155,216,542	676,711	155,893,254	76.00%	0.77%	0.69%	
TOTAL OPERATING FUNDS	**$ 204,805,287**	**$ (348,757)**	**$ 204,456,529**	**$676,711**	**$ 205,133,240**	**100.00%**			
Bond Fund Portfolios									
2011 Civic Center COPs	$ 7,838,995	$ -	$ 7,838,995	$ -	$ 7,838,995	59.63%	0.01%	0.01%	
Assessment Districts	2,211,870	-	2,211,870	-	2,211,870	16.82%	0.01%	0.01%	
Special Improvement Districts	3,096,212	-	3,096,212	-	3,096,212	23.55%	0.01%	0.01%	
TOTAL BOND FUNDS WITH FISCAL AGENT	**$ 13,147,076**	**$ -**	**$ 13,147,076**	**$ -**	**$ 13,147,076**	**100.00%**			
TOTAL CASH & INVESTMENTS	**$ 217,952,363**	**$ (348,757)**	**$ 217,603,606**	**$ 676,711**	**$ 218,280,317**				

The City's investment portfolio is expected to generate a return of a benchmark that most closely corresponds to the portfolio's duration, universe of allowable securities, risk profile and other relevant characteristics. The City's medium-term portfolio average annual total return fell from 1.22% to 0.21% during the fiscal year, while the benchmark's total return fell from 1.06% to 0.66%. This is largely attributable to a monthly loss in May and June of -0.27% and -0.35%, respectively, due to rapidly rising interest rates.



	QTR#1	QTR#2	QTR#3	QTR#4	MAY	JUNE	Fiscal Year 2011-12	Fiscal Year 2012-13
Medium-Term Total Return	0.39%	0.12%	0.19%	-0.48%	-0.27%	-0.35%	1.22%	0.21%
Index Total Return	0.48%	0.14%	0.18%	-0.14%	-0.15%	-0.12%	1.06%	0.66%
Excess Total Return	-0.09%	-0.03%	0.01%	-0.35%	-0.12%	-0.23%	0.16%	-0.45%

City of Newport Beach Medium-Term Portfolio										
	Medium-Term			Chandler		Cutwater		PFM		
Month	Market Value	Duration	Total Return	Duration	Total Return	Duration	Total Return	Duration	Total Return
July	163,172,824	1.698	0.277%	1.675	0.278%	1.615	0.275%	1.800	0.277%
August	154,469,444	1.610	0.065%	1.584	0.071%	1.455	0.068%	1.766	0.054%
September	151,933,613	1.746	0.043%	1.747	0.050%	1.682	0.046%	1.798	0.034%
October	151,907,166	1.833	-0.017%	1.771	0.005%	1.952	-0.019%	1.792	-0.037%
November	148,086,476	1.840	0.119%	1.736	0.107%	1.889	0.146%	1.902	0.108%
December	148,112,054	1.789	0.017%	1.697	0.006%	1.860	-0.014%	1.818	0.058%
January	148,114,928	1.855	0.009%	1.746	0.009%	1.979	-0.016%	1.854	0.031%
February	148,330,457	1.729	0.139%	1.728	0.143%	1.688	0.182%	1.767	0.095%
March	148,393,672	1.848	0.043%	1.800	0.031%	1.981	0.075%	1.777	0.025%
April	162,596,924	1.801	0.133%	1.620	0.148%	2.218	0.151%	1.570	0.101%
May	160,598,855	1.884	-0.266%	1.794	-0.229%	2.111	-0.439%	1.747	-0.128%
June	159,536,221	1.963	-0.351%	1.715	-0.256%	2.453	-0.673%	1.722	-0.122%
Fiscal Year	**153,771,053**	**1.800**	**0.211%**	**1.718**	**0.363%**	**1.907**	**-0.222%**	**1.776**	**0.497%**

Although all investments contain an element of risk, the City's Investment Policy is designed to limit exposure to risk. Each of the three professional investment advisors has unique strategies to minimize risk and take positions on key variables within the constraints of the City's investment policy. Despite the City realizing negative returns throughout the fiscal year, the medium-term portfolio has historically fell between the 1-3 Year Treasury index and 1-3 Year Government/Corporate AAA-A Rated benchmarks as indicated in the table below.

Total Rate of Return As of 06/30/2013	Current Month	Latest 3 Months	Annualized 1 Yr	3 Yrs	5 Yrs	10 Yrs
Chandler	-0.22%	-0.31%	0.37%	1.20%	2.52%	2.99%
Cutwater	-0.77%	-0.99%	-0.24%	0.61%	1.94%	2.78%
PFM	-0.10%	-0.14%	0.50%	1.15%	2.45%	2.95%
1-3 Yr Treasury	-0.07%	-0.11%	0.33%	0.82%	1.90%	2.59%
1-3 Gov/Corp A or Above	-0.12%	-0.14%	0.66%	1.17%	2.24%	2.78%

A more robust summary of portfolio characteristics and performance by each investment advisor is summarized and attached for your review.

Prepared by:

/s/Cory Pearson
Cory Pearson
Accountant

Submitted by:

/s/Dan Matusiewicz
Dan Matusiewicz
Finance Director

Attachments: A. FY 2012-13 Summary of Medium-Term Investment Portfolio Characteristics

Medium-Term Investment Portfolio Characteristics

Average FY2012-13

Summary	Chandler	Cutwater	PFM	1-3 Yr Gov/Corp AAA-A
Cash	1,848,223	1,226,718	473,061	N/A
Fixed Income	56,411,499	53,054,587	57,962,067	N/A
Duration*	1.715	2.453	1.722	1.905
Weighted Avg Life*	1.768	2.638	1.843	N/A
Weighted Avg Maturity*	1.810	2.990	1.816	1.966
Weighted Avg Eff Maturity*	1.740	1.803	1.766	1.966
Avg Credit Rating*	AA	AA-	AA	AAA
Yield to Maturity @ Market*	1.014%	0.788%	0.467%	N/A
Yield to Maturity @ Cost*	0.555%	1.011%	0.464%	0.538%
*** as of 06/30/13**				

Duration Allocation	Chandler	Cutwater	PFM	1-3 Yr Gov/Corp AAA-A
0.00 - 0.25	20.32%	24.63%	6.28%	0.25%
0.25 - 0.50	8.56%	0.52%	0.12%	0.15%
0.50 - 0.75	11.92%	5.21%	7.24%	0.41%
0.75 - 1.00	6.67%	10.43%	6.22%	4.37%
1.00 - 2.00	25.53%	20.97%	65.74%	55.90%
2.00 - 3.00	18.22%	15.83%	14.23%	38.92%
3.00 - 4.00	6.95%	13.57%	0.18%	0.00%
4.00 - 5.00	1.83%	8.85%	0.00%	0.00%
Total %	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Security Type Allocation	Chandler	Cutwater	PFM	1-3 Yr Gov/Corp AAA-A
Agency	47.96%	61.91%	42.72%	18.04%
Agency Discount Note	0.55%	0.00%	0.00%	0.00%
Asset-Backed Security	1.71%	0.00%	0.00%	0.00%
Cash	0.20%	0.44%	0.31%	0.00%
Commercial Paper	3.31%	0.08%	0.48%	0.00%
Corporate Notes	26.55%	27.17%	14.66%	15.33%
MM Fund	1.46%	1.98%	1.31%	0.00%
Municipal Bonds	0.00%	0.00%	1.11%	0.54%
U.S. Government	18.26%	8.43%	39.42%	66.10%
Total %	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Market Sector Allocation	Chandler	Cutwater	PFM	1-3 Yr Gov/Corp AAA-A
Agency	48.51%	61.91%	42.72%	18.04%
Asset Backed	1.71%	0.00%	0.00%	0.00%
Cash	1.66%	2.42%	1.62%	0.00%
Financial	16.34%	18.24%	9.64%	8.69%
Government	18.26%	8.43%	39.42%	66.10%
Industrial	13.21%	9.00%	5.50%	6.21%
Municipal	0.00%	0.00%	1.11%	0.54%
Utility	0.31%	0.00%	0.00%	0.43%
Total %	**100.0%**	**100.0%**	**100.0%**	**100.0%**

CITY OF NEWPORT BEACH
FINANCE COMMITTEE STAFF REPORT

July 22, 2013

TO: HONORABLE CHAIR AND MEMBERS OF THE COMMITTEE

FROM: Finance Department
Dan Matusiewicz, Finance Director
(949) 644-3123 or Danm@newportbeachca.gov

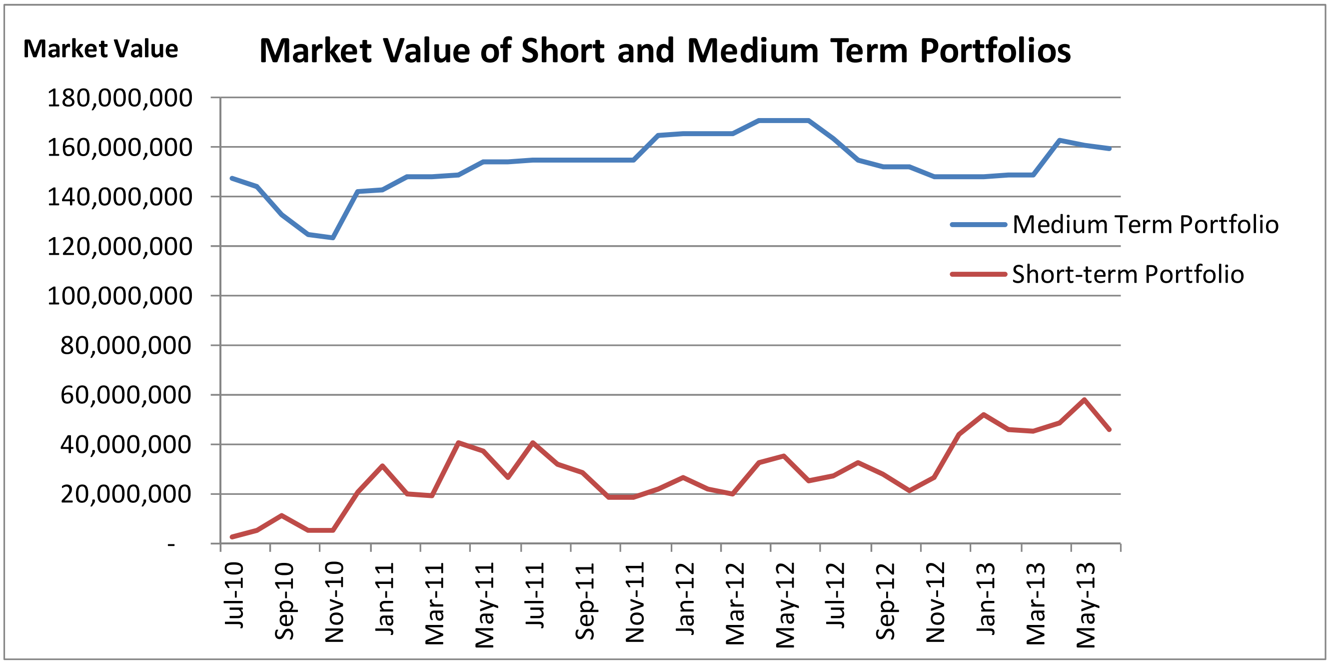
SUBJECT: **INVESTMENT STRATEGY REVIEW**

ABSTRACT:

The City's short-term investment portfolio has grown in recent years relative to the medium-term investment portfolio in order to provide sufficient liquidity for funding large scale capital projects. This has diluted the average duration of the medium term portfolio. Staff recently met with the City's investment advisors to discuss investment strategy and the following three strategies were considered: 1) create a new actively managed short-term portfolio, 2) consider increasing the duration of the City's medium-term portfolio when market conditions are favorable, and 3) establish benchmarks that generally represent the universe of investable securities for both the short-term and medium-term portfolios. Combined, the first two strategies will better manage short-term cash flow demands without causing undue disruption in the investment strategies of the medium-term portfolio, while the third strategy will provide meaningful reference points for evaluating portfolio performance. Finance staff is seeking feedback and/or approval on the investment management strategies and recommendations discussed below.

DISCUSSION:

The Council has directed staff in recent years to pursue an ambitious agenda to rehabilitate, replace, or develop new community serving facilities. This initiative has necessitated an increase in the amount of funds the City maintains in its short-term investment portfolio. The short-term investment portfolio provides a readily available source of funds to pay for the City's short-term liquidity needs. These short-term funds have traditionally been held in the State Treasury administered Local Agency Investment Fund (LAIF), which offers daily liquidity and low volatility due to the relatively short duration. The shorter duration also results in a commensurately lower return. The quarter ended June 30, 2013 LAIF yield was approximately 0.25% (See Exhibit A). Prior to the recent construction activities related to the Civic Center, the City's the short-term investment portfolio averaged $20M. In recent years it has increased up to anywhere between $45M and $60M, based on both current and anticipated liquidity needs related to the capital improvement projects identified in the Facilities Financing Planning Program . This change has resulted in the dilution of the portfolio's overall duration. The chart below demonstrates the increasing balance of the short-term portfolio relative to the medium-term portfolio.



Funds that are unlikely to be spent in the foreseeable future are kept in a medium-term investment portfolio actively managed by three individual investment advisors in accordance with all applicable City policies and codes, State statutes, and Federal regulations. Finance staff is tasked with efficiently managing the short-term cash flow demands without causing undue disruption to the investment strategies of the medium-term portfolio. This task is made more difficult in our current rising interest rate environment where investment losses may result if securities are liquidated prior to maturity. An over-reliance on cash flow from the medium-term portfolio may hinder the investment advisors' ability to achieve the benchmark rate of return, seize market opportunities, or rebalancing the portfolio.

Finance staff recently met with all three investment advisors to discuss alternative approaches to balancing the needs and objectives of the short-term and medium-term portfolios with a strategy that also optimizes yield. There was consensus among the advisors and staff that the following strategies are worthy of consideration:

Strategy Consideration 1 – Create an Actively Managed Segment of the Short-Term Portfolio

This strategy would assign one of the City's existing advisors the responsibility of buying securities with specific maturity dates to meet the short-term (operating and capital) cash flow demands of the City, and establish a suitable performance benchmark comparable with the characteristics of the portfolio. Staff would work with advisors to further develop schedules for cash out-flows related to major capital projects, and refine our cash forecasting techniques to minimize short-term portfolio balances.

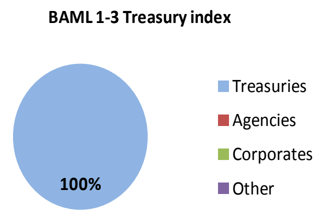
Strategy Consideration 2 – Increase the Duration of the Medium-Term Investment Portfolio

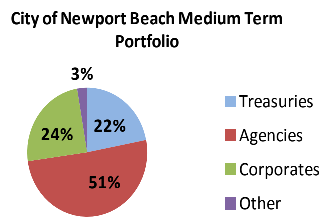
Since the gradual increase of the short-term portfolio balance dilutes the portfolio's overall duration and opportunity for investment return, staff believes that extending the duration of our medium-term portfolio to a 1-5 year duration could also produce desirable results over the long-term. A large component of the City's portfolio does not rely on immediate liquidity due to reserve restrictions, long-term funding programs and permanent endowments so the additional short-term volatility associated with a longer duration strategy is fiscally tolerable.

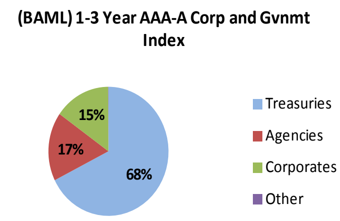
A comparative risk/benefit analysis of duration's impact on total return was prepared on a $50M segment of the City's investment portfolio over a 5 and 10 year period in Exhibits B & C respectively. In the ten year example, a 1-3 year Treasury-only strategy realized an annual return of 2.59% and experienced negative returns 7 out of 40 quarters. The 1-5 year Treasury-only strategy realized a 3.08% annual return but experienced negative returns 12 of 40 quarters. The City's current strategy of an actively managed 1-3 year portfolio produced a 2.95% return and experienced negative returns only 5 out of 40 quarters. Exhibit D further demonstrates a simulated shock analysis comparing the 1-3 yr and 1-5 yr strategies over four consecutive quarters. While we believe the City has the fiscal discipline and wherewithal to endure short-term interest rate volatility, due to the current rising interest rate environment, staff recommends revisiting this option in a year, or when market conditions exist that indicate a more stable environment. If such a strategy is deployed in the future, staff recommends incrementally extending the duration over time in order mitigate interest rate risk.

Strategy Consideration 3 - Establish Generally Representative Benchmarks for the Medium-Term Portfolio

The City has evaluated portfolio performance against a Treasury-only Index even though historically, the portfolio has also included government sponsored agency and corporate securities. Since the composition of the City's portfolio most often differs from a Treasury-only investment strategy, this type of benchmark does not always provide an apples to apples comparison. Staff is considering an alternative benchmark that more closely resembles the City's current investment mix. Staff recommends that the performance of the City's investments be compared to the total return that most closely corresponds to the portfolio's duration, universe of allowable securities, risk profile, and other relevant characteristics. Based on the composition of the available alternatives, staff believes the Bank of America Merrill Lynch (BAML) 1-3 Year AAA-A Corporate and Government Index (Bloomberg index number "B110") is more generally representative of our medium turn portfolio as demonstrated in the charts below:







<u>Summary Actions to Implement the Strategies</u>

Finance staff is seeking input from the Finance Committee on the proposed investment strategies described above and the following specific actions:

1. Create a new custodial account at the Bank of New York so that one of the City's current investment advisors can buy securities with specific maturity dates to meet the short-term cash flow demands of the City associated with larger construction projects and seasonal cash flow needs. This alternative would only be exercised when it can be demonstrated that the City's investment objectives can be better achieved with individual short-term securities compared to alternatives such as LAIF or other local government investment pools.

2. Maintain the current duration for the medium-term portfolio at 1-3 years and revisit extending the duration to a 1-5 year strategy in a year or so, or when market conditions are more stable.

3. Recognize and utilize the BAML 1-3 Year AAA-A Corporate and Government Index (Bloomberg index number "B110") and the BAML 1-3 Treasury Index as reference points to assess the performance of the City's medium-term portfolio. Taken together, these benchmarks better represent the duration, universe of allowable securities, risk profile, and other relevant characteristics of the City's medium term investment portfolio.

4. Utilize a short-term performance benchmark such as the BAML 91 day Treasury Index and the BAML 0-1 Year Treasury index that best corresponds to the City's short-term portfolio characteristics to assess the performance of the City's short-term investment portfolio strategy.

In consultation with the City's investment advisors, Finance Staff recommends consideration of these changes because they allow staff to better manage short-term cash flow demands without causing undue disruption in the investment strategies and provide meaningful reference points for evaluating the performance of the City's investment portfolio.

Prepared by:	Submitted by:
/s/Sandra Wilcox	/s/Dan Matusiewicz
Sandra Wilcox	Dan Matusiewicz
Senior Accountant	Finance Director

Exhibits:
A. LAIF Performance Report
B. Risk/Return Comparisons of Various Benchmarks (5 Years)
C. Risk/Return Comparisons of Various Benchmarks (10 Years)
D. Interest Rate Shock Analysis

Exhibit A

Bill Lockyer, State Treasurer

Inside the State Treasurer's Office

Local Agency Investment Fund (LAIF)

LAIF CONFERENCE INFORMATION

PMIA Performance Report

Date	Daily Yield*	Quarter to Date Yield	Average Maturity (in days)
7/2/2013	0.26	0.26	297
7/3/2013	0.26	0.26	295
7/4/2013	0.26	0.26	295
7/5/2013	0.26	0.26	293
7/6/2013	0.26	0.26	293
7/7/2013	0.26	0.26	293
7/8/2013	0.26	0.26	292
7/9/2013	0.26	0.26	294
7/10/2013	0.26	0.26	295
7/11/2013	0.26	0.26	293
7/12/2013	0.27	0.26	297
7/13/2013	0.27	0.26	297
7/14/2013	0.27	0.26	297
7/15/2013	0.27	0.26	295

*Daily yield does not reflect capital gains or losses

LAIF Performance Report

Quarter ending 06/30/2013

Apportionment Rate:	0.24%
Earnings Ratio:	00000667321954799
Fair Value Factor:	1.000273207
Daily:	0.25%
Quarter To Date:	0.25%
Average Life:	278

PMIA Average Monthly Effective Yields

JUNE 2013	**0.244%**
MAY 2013	0.245%
APRIL 2013	0.264%

Pooled Money Investment Account
Portfolio Composition
$58.8 Billion
06/30/13

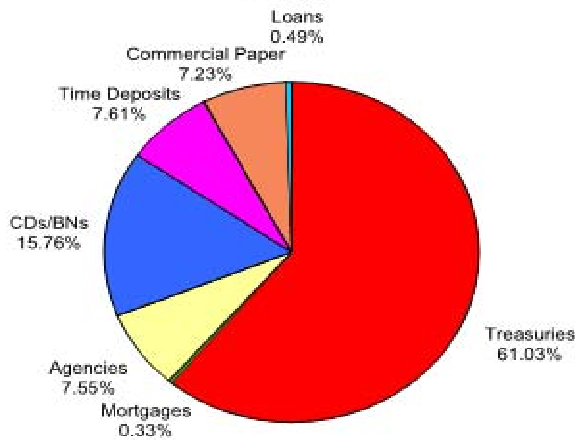


Exhibit B

Risk/Return of Various Benchmarks 5 Years Ended June 30, 2013				
Merrill Lynch Index	**Duration (years)**	**Annualized Total Return**	**Cumulative Value of $50 Million**	**Quarters With Negative Return**
LAIF	0.58	0.80%	$52,029,300	0 out of 20
1-3 Year Treasury	1.81	1.90%	$54,929,600	4 out of 20
City of Newport Beach Current Strategy	1.79	2.45%	$56,423,100	2 out of 20
1-5 Year Treasury	2.64	2.77%	$57,327,400	6 out of 20

Source: Bloomberg, Bank of America Merrill Lynch

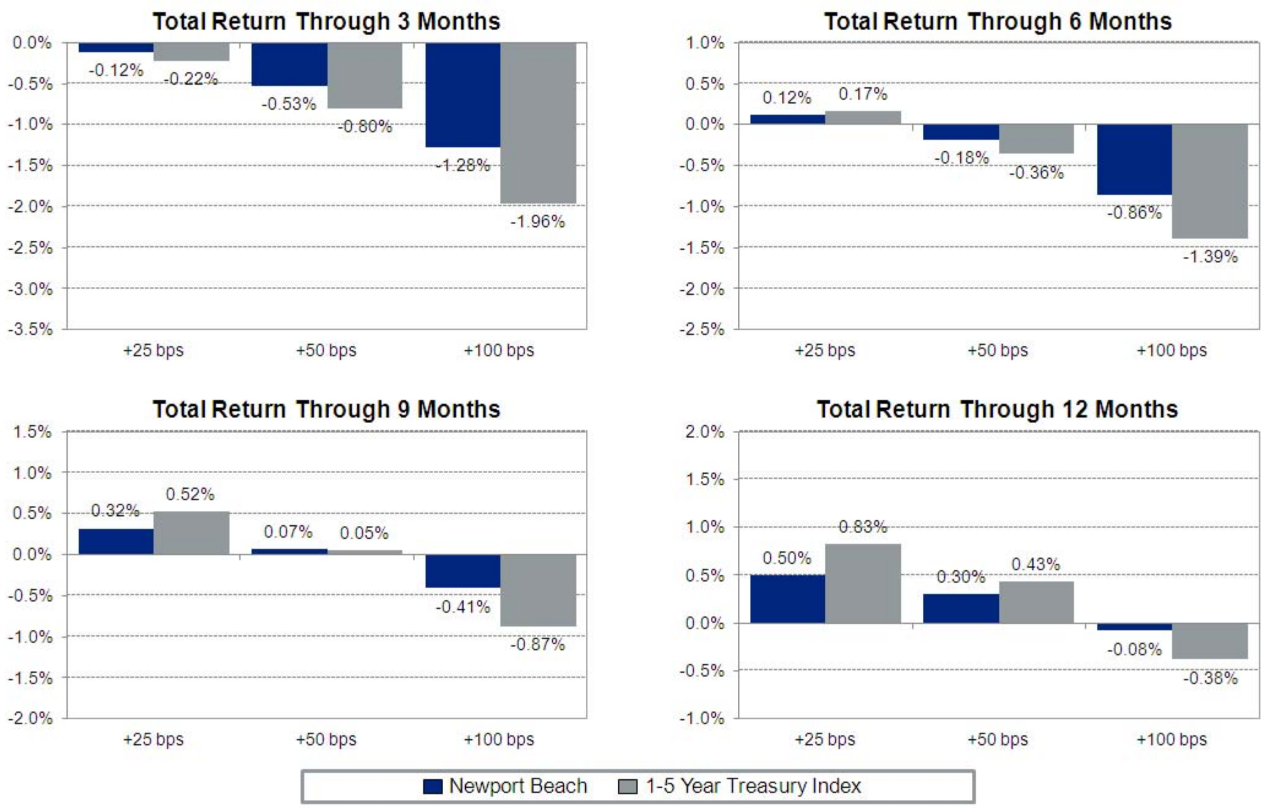
Exhibit C

Risk/Return of Various Benchmarks 10 Years Ended June 30, 2013				
Merrill Lynch Index	**Duration (years)**	**Annualized Total Return**	**Cumulative Value of $50 Million**	**Quarters With Negative Return**
LAIF	0.58	2.09%	$61,752,100	0 out of 40
1-3 Year Treasury	1.81	2.59%	$64,564,500	7 out of 40
City of Newport Beach Current Strategy	1.79	2.95%	$66,905,200	5 out of 40
1-5 Year Treasury	2.64	3.08%	$67,722,500	12 out of 40

Source: Bloomberg, Bank of America Merrill Lynch

Exhibit D

Forward Looking Interest Rate Shock Analysis
Newport Beach -Current Strategy



Analysis performed with data as of June 30, 2013.
Base level security pricing was provided in the City's statement.
Historical yield curves, as of June 30, were used for U.S. Treasuries, federal agencies and corporate securities independently and with the relevant yield curve applied to each investment by sector.
Yields for maturities between yield curve points were interpolated using cubic interpolation methods.
Interest rate shifts are parallel and applied to the base yields as of June 30, 2013.
Fair market values and accrued interest values were determined using industry standard calculation methods.
Assumes that each interest rate scenario occurs gradually over the course of the tested time period.
Excludes reinvestment of maturities and coupon payments.
Benchmark does not include Corporate AAA to A in order to isolate the risk due to Duration.