

**CITY COUNCIL RESOLUTION NO. 60-16**

**A RESOLUTION OF THE COUNCIL OF THE CITY OF RICHMOND, CALIFORNIA,  
ADOPTING THE DEBT POLICY, SWAP POLICY AND CASH RESERVE POLICY  
FOR FISCAL YEAR 2016-17**

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**WHEREAS**, the City of Richmond (the “Authority”) is a charter city that operates under the Council-Manager form of government for the purposes of providing a full range of municipal services including police and fire protection; construction and maintenance of highways, streets and infrastructure; library services; storm water and municipal sewer systems; a wastewater treatment facility; and the administration of recreational activities and cultural events; and

**WHEREAS**, the Authority also operates the Richmond Memorial Convention Center and the Port of Richmond; and

**WHEREAS**, the Authority has established and maintains a well-managed debt program pursuant to a comprehensive debt policy that sets forth the parameters for issuing debt and managing the debt portfolio, including post-issuance compliance; and

**WHEREAS**, and in the credit rating process, the rating agencies believe it is appropriate to place significant value on debt policies that have been adopted by cities; and

**WHEREAS**, the Authority established a Debt Policy that requires annual commitments relating to the General Fund debt cannot exceed ten percent (10%) of annual General Fund revenues; and

**WHEREAS**, the Authority has established interest rate swap agreements that are recognized as financial tools by municipal issuers throughout the nation and the use of swap agreements has become a regular tool whereby the Government Finance Officers Association (GFOA) has adopted an official position, viewing swap policies as a governing use and management of such swaps as a “Recommended Practice”; and

**WHEREAS**, the Authority has established that the scope of interest rate swaps is beyond that of the traditional fixed rate long-term bonds covered by the Debt Policy and that it is important for the City to maintain a policy that will provide guidance in selecting, implementing, and administering all swaps related to City bond issues; and

**WHEREAS**, the Authority established a Swap Policy whereby Standard & Poor’s (S&P) Rating Agency assigns a Debt Derivative Profile (DDP) in which the City has achieved a DDP score of “1.5” (low risk) on all of its swap transactions; and

**WHEREAS**, the Authority has determined that an appropriate level of the General Fund reserves is a policy decision; and

**WHEREAS**, the GFOA recommends that reserve levels be directly related to the degree of uncertainty the local government faces; and

**WHEREAS**, the Fiscal Year 2016-17 Cash Reserve Policy identifies an ending cash balance equal to seven percent (7%) of the General Fund expenditures as the minimum needed to provide stability against potential volatility of revenues and uneven cash flows; and

**WHEREAS**, the adoption of the financial policies listed in this document is consistent with “best practices” and the Authority’s fiduciary oversight of the Fiscal Policies of FY2016-17.

**NOW, THEREFORE BE IT RESOLVED** that the City Council hereby adopts the Debt Policy for the City of Richmond that is attached hereto as Exhibit A.

**BE IT FURTHER RESOLVED** that the City Council also adopts the Swap Policy for the City of Richmond that is attached hereto as Exhibit B.

**BE IT FURTHER RESOLVED** that the City Council also adopts the Cash Reserve Policy for the City of Richmond that is attached hereto as Exhibit C.

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I certify that the foregoing resolution was passed and adopted by the Council of the City of Richmond at a regular meeting thereof held July 5, 2016, by the following vote:

AYES: Councilmembers Bates, Beckles, McLaughlin, Myrick, Pimplé, Vice Mayor Martinez, and Mayor Butt.

NOES: None.

ABSTENTIONS: None.

ABSENT: None.

PAMELA CHRISTIAN  
CLERK OF THE CITY OF RICHMOND  
(SEAL)

Approved:

TOM BUTT  
Mayor

Approved as to form:

BRUCE GOODMILLER  
City Attorney

State of California            }  
County of Contra Costa        } : ss.  
City of Richmond               }

I certify that the foregoing is a true copy of **Resolution No. 60-16**, finally passed and adopted by the City Council of the City of Richmond at a regular meeting held on July 5, 2016.

  
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Pamela Christian, Clerk of the City of Richmond

**Debt Policy of the City of Richmond  
Established by the Finance Department**

***Fiscal Year 2016-17***

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**Scope and Application**

*This Debt Policy, established by and for the Finance Department, pertains to financings under the jurisdiction of the City of Richmond Finance Department, the Richmond Housing Authority, the Successor Agency to the Richmond Community Redevelopment Agency, the Richmond Joint Powers Financing Authority and the City itself. This Policy is intended to guide the Finance Department in its debt issuance in the course of its customary practices. From time to time, certain circumstances arise which could cause the Finance Department to deviate from the policies herein.*

*This Policy and any subsequent amendments hereto shall be on file with the Finance Department and shall be, contained on the City's website, with copies delivered to the City Clerk and the City Council.*

**Mission of the Finance Department Treasury Division**

The Finance Department shall issue and manage short and long-term financings (bonds, TRANs, etc.), both for capital improvement and operating needs, by balancing market and credit risk with satisfactory economic benefits and proper fiscal controls. To achieve the mission goals, the Finance Department shall adhere to the following:

**I. Debt Management Objectives**

- The Finance Department shall maintain cost-effective access to the capital markets through prudent policies.
- The Finance Department shall maintain moderate debt and debt service payments with effective planning and coordination with City departments.
- The Finance Department shall meet significant capital demands through debt financing and alternate financing mechanisms such as public/private partnerships.
- The Finance Department shall achieve the highest possible credit ratings within the context of the City's capital needs and financing capabilities.

**II. Types and Purposes of Debt**

The Finance Department may utilize several types of municipal debt obligations to finance long-term capital projects. Long-term debt is only issued to finance the acquisition and/or construction of capital improvements unless otherwise decreed by court order or adjudicated settlement. Long-term debt financing shall never be used to fund operating or maintenance costs.

**Assessment Bonds** Proceeds from Assessment Bonds may be used to finance local public improvements, provided that said improvements benefit the parcels of land to be assessed. Local streets, street lights, landscaping, sidewalks and

sanitary sewers are some examples of local improvements commonly financed by assessment bonds.

**General Obligation Bonds** General Obligation Bonds may only be issued with two-thirds approval of a popular vote. The California State Constitution (Article XVI, Section 18) limits the use of the proceeds from GO Bonds to “the acquisition or improvement of real property.” Libraries, parks and public safety facilities are all types of facilities that could be financed with GO Bonds.

**Pension Obligation Bonds** Pension Obligation Bonds are issued to finance all or part of the unfunded pension liabilities of the City. Typically, these bonds are issued at a lower rate of return than was being paid to the Pension System Administrator, and in this way, provide an economic benefit to the City.

**Enterprise Revenue Bonds** Enterprise Revenue Bonds finance facilities for a revenue producing enterprise, and are payable from revenue sources within that enterprise. The Convention Center, KCRT Cable Television and Municipal Sewer are examples of revenue producing enterprises within the City.

**Lease Revenue Bonds** Lease Revenue Bonds are typically issued by the Joint Powers Financing Authority (JPFA) of the City, on behalf of the City. The site on which the project is being built is least to the JPFA and then the capital project being financed along with the site is leased back to the City. Alternatively, a different asset is leased to the JPFA and leased back, with the proceeds of the bonds being used for some other capital improvements (this is known as an “asset transfer” financing). The lease payments from the City are subsequently collected by the JPFA and used to fund the debt service payments. Internally, costs of particular projects can be allocated to the budgets of one or more departments, but the City’s general fund is liable to pay lease payments. Some other agencies that may issue these type of bonds are the Redevelopment Agency and the Parking Authority.

**Financing Leases** The City may finance a capital asset by leasing it directly from the vendor or leasing company, with the lessor receiving a portion of each rental payment as tax-exempt interest.

**Other JPFA Conduit Financings** In addition to Lease Revenue Bonds, the JPFA can assist in financing a wide variety of projects by issuing bonds secured by loan agreements, installment sale agreements, underlying assessment or Mello-Roos obligations and similar instruments. Such instruments can also be used to pool various financing projects into one JPFA bond issue.

**Mello-Roos Bonds** The City may issue bonds through a Community Facilities District (CFD). These bonds must be approved by a two-thirds vote of the registered voters within the district (unless there are fewer than 12 registered voters, in which case the vote is by the landowners), and are secured by a special

tax on the real property within the district. The bonds may be issued to finance facilities or provide services, although the facilities do not need to be physically located within the district.

**Tax Allocation Bonds** Using tax increment funds as a pledge for repayment, the Redevelopment Agency may issue Tax Allocation Bonds. Careful consideration must be taken by the Redevelopment Agency when issuing these bonds, to ensure that the revenue source is not already pledged to some other encumbrance, such as HUD loans.

**Refunding Obligations** Pursuant to the Government Code and various other financing statutes applicable in particular situations, the City Council is authorized to provide for the issuance of bonds for the purpose of refunding any long-term obligation of the City. Absent any significant non-economic factors, a refunding should produce minimum net debt service savings (net of reserve fund earnings and other offsets) of at least 3% of the par value of the refunded bonds on a net present value basis, using the refunding issue's True Interest Cost (TIC) as the discount rate, unless the Finance Director determines that a lower savings percentage is acceptable for issues or maturities with short maturity dates.

**Tax and Revenue Participation Notes** Tax and Revenue Anticipation Notes (TRANs) are routinely issued by the City to fund cash flow deficits in a fiscal year. TRAN proceeds may be used and expended for any purpose, including operating expenses, capital expenditure, repayment of indebtedness and investment and reinvestment.

Pursuant to Treasury Regulations, TRAN proceeds may be invested at an unrestricted yield if TRANs are issued in an amount not to exceed the maximum anticipated cumulative cash flow deficit over 13 months plus the lesser of either (i) a reasonable working capital reserve or (ii) 5% of the prior fiscal year's expenditures paid out of current revenues. The policy of the Finance Department is that TRANs shall only be issued in such amount as to satisfy said Treasury Regulations.

**Other Obligations** There may be special circumstances when other forms of debt are appropriate and may be evaluated on a case-by-case basis. Such other forms include, but are not limited to non-enterprise revenue bonds, bond anticipation notes, grant anticipation notes and judgment or settlement obligation bonds.

### **III. Debt Approval Procedures**

**A. Reviewed by City Council** All long-term financing proposed transactions for capital improvements shall be reviewed by the City Council. For matters related to the City Council approval process, "long-term financing" means financing which constitutes an obligation beyond one fiscal year.

1. Proposed transactions submitted for City Council approval should be reviewed prior to submission by the Finance Director, City Manager and City Attorney.
2. Upon approval by the Finance Director, City Manager and City Attorney, the proposed transaction shall then be presented to the full City Council.

**B. Approval by the City Council** All long-term financing transactions shall be approved and adopted by the City Council. The City Council shall comply with all public hearing requirements applicable to the specific type of bond being approved.

#### **IV. Debt Limitations**

There is no statutory restriction on the amount of Lease Revenue Bonds or COPs that can be outstanding at any given time. However, it is the policy of the City of Richmond that net debt service payments funded from General Fund sources shall be no greater than 10% of current General Fund revenues. Payments on bonds that are tied to a specified revenue stream other than General Fund sources (e.g. enterprise revenue bonds, tax allocation bonds and assessment bonds) are not subject to this 10% limit. Each proposed financing will be individually assessed by the Finance Department and subject to the approval policies contained herein.

The City also issues debt funded by revenues of Business-type activities, also known as Enterprise Funds. Any debt secured by revenues of an Enterprise Fund shall maintain a coverage ratio equal to 125% of net revenues of the Enterprise Fund.

#### **V. Methods of Sale**

The Finance Director shall review each transaction on a case-by-case basis to determine the most appropriate method of sale.

**A. Competitive Sale** In a competitive sale, bids for the purchase of the bonds are opened at a specified place and time and are awarded to the underwriter (or syndicate) whose conforming bid represents the lowest true interest cost to the City (TIC). The City may take bids in person, by facsimile, or by electronic means.

1. Bond sales shall be advertised as broadly as possible, including advertising in an industry newspaper. The financial advisors for each transaction shall undertake to market the bonds to prospective bidders and investors as relevant.
2. Terms of the bonds shall be amendable as late as possible and ideally until at least 1:00 p.m. Pacific Time the day prior to the day bids are to be received.
3. Bond sales shall be cancelable at any time prior to the time bids are to be received.
4. Upon award to the bidder whose conforming bid represents the lowest true interest cost, the City may restructure the bonds in accordance with the Official Notice of Sale.
  - i. The City shall reserve the unfettered right to reject all bids or waive bid irregularities.
  - ii. The Finance Director, or his designee shall award any bonds sold via competitive sale.

**B. Negotiated Sale** In a negotiated sale, the City chooses the initial buyer of the bonds in advance of the sale date. The initial buyer is usually an investment banking firm, or a syndicate of investment banking firms interested in reoffering the bonds to investors through an underwriting process. This type of sale allows the City to discuss different financing techniques with the underwriter in advance of the sale date, and is particularly appropriate for complex bond structures, difficult credit situations (such as non-rated assessment or Mello-Roos Bonds, and refunding's).

**C. Private Placement** Also referred to as a direct placement, private placement is a variation of a negotiated sale. Instead of retaining the services of an investment banking firm to underwrite the securities, the City will sell the bonds directly to a limited number of investors. The City may use a placement agent to assist it in identifying likely investors.

## VI. Debt Structuring Practices

**A. Standard Terms** The following terms shall be applied to the City's transactions as appropriate. Individual terms may change as dictated by the marketplace or the unique qualities of the transaction.

### 1. All Bonds

- i. Term 30 years is standard, but up to 35 years may be acceptable, depending on cash flow assumptions, construction timeline and remaining useful life of the asset being financed.
- ii. Maximum Yield not to exceed 12% for tax-exempt financings
- iii. Maximum Premium case by case, as recommended by the City's Financial Advisor.

- iv. Maximum Discount case by case, as recommended by the City’s Financial Advisor.
- v. Payment Dates - Fixed after considering cash flow needs, the Finance Director will determine the occurrence of all new debt service payments.
- vi. Coupons fixed rate or variable rate.
- vii. Call Provisions shortest possible optional call consistent with optimal pricing.
- viii. Structure of Debt prefer level debt service, but shall be determined on a case-by-case basis, at the discretion of the Finance Director.
- ix. Debt Service Reserve lesser of 10% principal amount, 125% average annual debt service, 100% maximum annual debt service or surety bond.
- x. Capitalized Interest sized through substantial completion plus a minimum of six months unless other assets are available to be pledged or otherwise limited under Federal Tax Law. Liquidated damages of construction contract must include amount of daily debt service.
- xi. Net Funding the project and capitalized interest funds may be net funded if investments are secured upon issuance of bonds.
- xii. Reimbursement Resolution Must be adopted by the City Council if the project hard costs are advanced by the General Fund prior to the bond sale.
- xiii. Good Faith Deposit determined on a case-by-case basis by the Finance Director.

**2. Variable Rate Bonds** The City may elect to issue any bonds as variable rate bonds, which are broadly defined to mean daily, weekly, monthly, semi-annual or auction rate.

- i. Purpose reduction of net borrowing cost; match of assets and liabilities.
- ii. Max Portfolio Allocation no more than 20% of the City’s outstanding debt portfolio shall be in un-hedged short-term paper consistent with policies for underlying debt types.
- iii. Term consistent with policies for underlying debt types

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| iv. Maximum Yield          | not to exceed 12%  |
| v. Monitoring              | the Finance Department shall monitor all variable rate bonds on a monthly basis and shall determine, from time to time, whether to change modes and/or replace a broker/dealer or remarketing agent.                         |
| vi. Budgeting              | the Finance Department will recommend that annual debt service on any variable rate bonds be budgeted at 1.5 times the rolling 3-year average of the Bond Market Association index, or another relevant index of time frame. |
| viii. Liquidity            | a liquidity facility shall be obtained, either externally or internally, for all short-term indebtedness containing a put feature.   |
| ix. Mode                   | all bonds issued as variable rate bonds shall be issued as “multi-modal” bonds.  |
| x. Good Faith Deposit      | determined on a case-by-case basis by the Finance Director.  |
| xi. Budgeting Debt Service | budget shall be 3-year BMA rolling average times 1.5 as well as ongoing fees associated with floating rate bonds.  |

## **VII. Derivatives Policy**

Derivative products and other financial instruments can be beneficial interest rate management tools that can assist the City as part of its overall debt and investment management program, but need to be monitored very closely. Derivative products may be used by the City to reduce risk exposures or reduce interest costs, but may not be used for speculative purposes. The City maintains a separate policy regarding its use of derivative products.

## **VIII. Permitted Investments**

All investments of bond proceeds shall adhere to the City’s Investment Policy, approved periodically by the City Council, as outlined in Appendix A. With the exception of guaranteed investment contracts, investments shall not allow security types or credit standards less than those of the City’s Investment Policy.

1. City of Richmond Investment Policy: attached hereto as Appendix A.
2. Investment Agreements (IAs)
  - i. Purpose
    - a) maximize interest earnings, thereby reducing net borrowing cost, b) match of assets and liabilities and/or c) hedging.

- ii. Counterparty minimum rating of AA- from S&P or Aa3 from Moody's.
- iii. Mandatory Termination limited to credit-related events and non-payment.
- iv. Cure Provisions timelines on City's obligations to cure must provide for appropriate legislative action.
- v. City's Priority of Payment termination payments – subordinate to related debt payments.
- vi. Procurement/Award award based on best bid as defined in bid form after limited negotiation of terms.
- vii. Term not in excess of the term of the bonds.

## IX. Professional Assistance

- A. **Financial Advisors** The City shall utilize the services of independent financial advisor(s) on debt financing when deemed prudent by the Finance Director. The City may utilize an RFP-selected pool of such financial advisors to mitigate time constraints and reduce overhead costs of the City in procuring such services. Services shall be documented by contract and compensation shall be capped.
- B. **Underwriters** In the case of a competitive sale, the City will award the bonds to the underwriting firm whose bid results in the lowest True Interest Cost. In the case of a negotiated sale, the Finance Director will determine the best method of selection, taking into consideration all factors involved in each particular sale.
- C. **Bond Counsel** The Finance Department, in consultation with the City Attorney's Office, shall select bond counsel for each transaction.
- D. **Broker-Dealers and Remarketing Agents** For all variable rate bonds, the Finance Director shall select broker-dealers or remarketing agents for each transaction. The City shall monitor performance on a monthly basis. The City may replace a remarketing agent or broker-dealer with notice at any time.
- E. **Trustees** Selected for each transaction by RFP, unless use of current trustee is deemed practical by the Finance Director. The Trustee (or applicable holding company) shall have a combined capital and surplus of at least \$50,000,000 and be subject to supervision or examination by federal or state authority.
- F. **Rebate Consultant** Selected by RFP for all bonds for a set term with 1-year extensions.
- G. **Financial Printer** Selected for each issue by RFP.

- H. Auction Agents** Selected for each relevant issue by RFP issued by the Finance Department or its agent and subject to negotiation of terms.
- I. Liquidity Providers** Selected for each relevant issue by RFP issued by the Finance Department or its agent and subject to negotiation of terms.
- J. Investment Agreement Counterparties** Selected by bid in compliance with Federal Tax Law Requirements in accordance with relevant bond documents and the City's Investment Policy.
  - 1. In general, uncollateralized Investment Agreements shall be executed with counterparties rated at least AAA with collateral required upon downgrade below AAA.
  - 2. Repurchase Agreements or Forward Delivery Agreements shall be executed with counterparties rated at least AA (by at least one of the major rating agencies) with downgrade provisions requiring assignment or collateral should the rating fall below A- or A3 by Standard and Poor's or Moody's Investor Services respectively.

**X. Ongoing Debt Administration**

- A. Continuing Disclosure** It is the goal of the Finance Department to be as transparent as possible.
  - 1. Annual Report. The City will covenant to provide its annual disclosure report no later than 270 days following the end of the fiscal year. However, the City will use its best efforts to issue the Annual Report as soon as practical following the issuance of the City's annual Comprehensive Annual Financial Report (CAFR). The City shall use its best efforts to issue the Annual Report electronically and to post the Annual Report on its web site. The Annual Report will also be on file with the City Clerk.
  - 2. Material Event. The City will issue a material event notice in accordance with the provisions of SEC Rule 15c2-12. Prior to the issuance of any material event, the Finance Director will convene a meeting of the Mayor, City Manager, City Attorney and policymakers or outside professionals as appropriate, to discuss the materiality of any event and the process for equal, timely and appropriate disclosure to the marketplace.
  - 3. Post-Issuance Compliance on Build America Bonds. The City will adhere to the instructions contained in Appendix B regarding required post-issuance activities when Build America Bonds have been issued.

Upon recommendation of the Finance Director, the City may retain a firm to assist it in maintaining compliance with all continuing disclosure requirements.

- B. Arbitrage Rebate Compliance** The City shall calculate arbitrage annually in each year that the related construction fund (or equivalent) has had an outstanding balance. Thereafter, the City shall calculate arbitrage on the fifth anniversary of the bond issuance in accordance with IRS recommended practices.
- C. Insurance Certifications** The City (through its Risk Manager) shall provide annual insurance certification to the Trustee and Bond Insurer, if required under the legal documents for each issue.
- D. Ratings** The policy of the Finance Department is to secure underlying ratings on all newly issued obligations from at least one national rating agency.
1. Annual Meeting. The Finance Department shall meet with each rating agency that rates City debt issues at least annually unless such meeting is declined by the respective rating agency.
  2. Reporting. The Finance Department shall ensure prompt delivery to each of the rating agencies of the following public documents:
    - i. Annual CAFRs
    - ii. Annual proposed budgets
  3. Other Reporting Certificates of Substantial Completion on projects financed with long term obligations shall be delivered to the rating agencies and Bond Insurer, as relevant.
  4. Citywide Ratings Notification Any changes in ratings will be promptly noticed to the Mayor and the City Council.





## APPENDIX A

### CITY OF RICHMOND INVESTMENT POLICY FY16-17

#### **I. Mission Statement**

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

#### **II. Policy**

The investment policy shall be adopted by resolution of the City Council. The policy shall be reviewed annually by the Council and any modification made thereto must be approved by the City Council.

#### **III. Delegation of Authority**

Management responsibility for the investment program is hereby delegated to the Director of Finance who shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials, and their procedures in the absence of the Director of Finance.

#### **IV. Scope**

This Statement addresses the investment policy for the City's pooled funds. The pooled funds include the General Fund, Special Revenue, Debt Service, Capital Projects, Enterprise, Internal Service, Trust & Agency, Successor Agency and any other Funds authorized by the City Council which are accounted for in the City of Richmond Comprehensive Annual Financial Report (CAFR).

The investment policy for bond and note proceeds is contained in the bond documents approved by the City Council at the time of the issuance of the debt; provided that, to the extent not inconsistent with such bond documents, bond or note proceeds, and in accordance with the Government Code Sections 53601(l) and 5922(d), may be invested in (i) Guaranteed Investment Contracts or other debt issuance proceeds with an investment provider rated in a category of "A" or better and with downgrade protection or (ii) Investment instruments described herein.

The investment policy for the Police and Fire Pension Fund and the General Pension Fund are contained in the City Charter.

## V. Objectives

The City's investment activities are designed to accurately monitor and forecast expenditures and revenues in order to:

1. Invest up to 100% of all idle funds.
2. Guarantee that funds are always available when needed.
3. Manage the portfolio in order to take advantage of changing economic conditions that can aid in increasing the total return on the City's portfolio.
4. Safety. The primary duty and responsibility of the Treasurer is to protect, preserve and maintain cash and investments placed in his/her trust on behalf of the citizens of the community. To attain this objective, the City will diversify its investments by investing funds among a variety of securities offering independent returns and financial institutions.
5. Liquidity. An adequate percentage of the portfolio should be maintained in liquid short-term securities that can be converted to cash if necessary to meet disbursement requirements. Since all cost requirements cannot be anticipated, investment in securities with active secondary or resale markets is highly recommended. Emphasis should be on marketable securities with low sensitivity market risks.
6. Yield. Yield, sometimes referred to as "rate of return," is the potential dollar earnings investment can provide. Yield should become a consideration only after the basic requirements of safety and liquidity have been met with measurement of investment risk and the cash flow needs.

## VI. Ethics and Guidelines

1. The City adheres to the guidance provided by the "prudent investor standard".  
"A standard of conduct where a person acts with care, skill, prudence, and diligence when investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing funds. The test of whether the standard is being met is if a prudent person acting in a similar situation would engage in similar conduct to ensure that investments safeguard principal and maintain liquidity."
2. All participants in the investment process shall act as custodians of public trust. Investment officials shall recognize that the investment portfolio is subject to public review and evaluation. The overall program shall be designed and managed with a degree of professionalism that is worthy of the public trust.

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<sup>1</sup>As defined in the California Debt Advisory Commission's October 1996 document: *Local Agency Investment Guidelines: Recommendations for Implementing Recent Statutory Changes to the California Government Code Sections 16429.1 and 53600 through 53684.*

3. In a diversified portfolio it must be recognized that occasional measured losses are inevitable and must be considered within the context of the overall portfolio investment return provided that adequate diversification has been implemented. Each issuer shall be limited in terms of their percentage of the portfolio, to minimize risk exposure.
4. In accordance with California Government Code Sections 89502 and 89503, officers and employees of the City shall refrain from any activity that could conflict with the proper execution of the investment program or that could impair their ability to make impartial investment decisions. All investment personnel shall comply with the reporting requirements of the Political Reform Act, to include the annual filing of a Statement of Economic Interest.

## **VII. Reporting and Review of the Investment Portfolio**

The Director of Finance shall report monthly on the City's pooled and Bond funds to the City Manager and City Council and shall report quarterly on other investments, such as, pension funds. The following elements will be part of the investment report:

1. Type of investment
2. Institution/Issuer
3. Date of maturity
4. Cost of security (par amount) and dollar amount in all securities
5. Description of the funds, investments and programs managed by contracts
6. Current market value of all securities
7. Rate of return
8. Statement of compliance to meet its pool expenditure requirements for the next six months
9. If, in any case, pool expenditures are not met, an explanation of why sufficient monies will not be available.

## **VIII. Internal Control**

The Treasurer or designee shall maintain a system of internal controls designed to ensure compliance with the Investment Policy and to prevent losses due to fraud, employee error, and misrepresentations by third parties or unanticipated changes in financial markets.

## **IX. Authorized Broker/Dealers**

The Director of Finance will maintain a list of broker/dealers authorized to provide investment services. The broker/dealers will be selected by credit worthiness that is authorized to provide investment services in the State of California. These may include "primary" dealers or "regional" dealers that qualify under Securities and Exchange Commission Rule 15C3-1 (uniform net capital rule).



All financial institutions and broker/dealers who desire to become qualified bidders for investment transactions must supply the Director of Finance with the following: audited financial statements, proof of FINRA certification, and proof of state registration, completed broker/dealer questionnaire, and certification of having read the City's investment policy.

An annual review of the financial condition and registrations of qualified bidders will be conducted by the Director of Finance. The bidding process shall be conducted every five years. The current audited financial statement is required to be on file for each financial institution and broker/dealer in which the City invests.

## **X. Authorized Investments and Maximum Maturities**

With the above objectives and criteria in mind, the City of Richmond may invest in the following instruments that have maturities of five (5) years or less at the time of purchase, unless otherwise stated below:

1. Government Bonds and Notes – Maximum of 100% invested no longer than 5 years
  - i. United States Treasury Notes, Bonds, Bills, or certificates of indebtedness or those for which the full faith and credit of the United States are pledged for the payment of principal and interest;
  - ii. Treasury notes or bonds of the State of California; and
  - iii. Bonds, Notes, Warrants or other evidences of indebtedness of any local agency within California, rated in a rating category of "A" or better by a nationally recognized rating service.
2. Bonds and Notes of Federally Sponsored Agencies – Maximum of 90% invested no longer than 5 years, such as the Federal Farm Credit Bank, Federal Home Loan Bank, Federal National Mortgage Association, Government National Mortgage Association or any other instruments issued by a federal agency or a United States government sponsored enterprise.
3. Negotiable Certificates of Deposit issued by a Federal and State chartered bank or a Federal and State Savings and Loan Association or by any state licensed branch of a foreign bank. Purchases are not to exceed 20% of invested idle funds.
4. Local Agency Investment Fund (LAIF) – maximum of \$50 million per account. The City may invest in the Local Agency Investment Fund (LAIF) established by the State Treasurer for the benefit of local agencies up to the maximum permitted by State law.



5. Medium Term Corporate Notes with a maximum of five years maturity issued by corporations organized and operating within the United States. Such securities must be rated in a rating category of “A” or better by a nationally recognized rating service. Purchases may not exceed 30% of invested idle funds.
6. Commercial Paper of “prime quality” of the highest ranking or of the highest letter and numerical rating as provided for by Moody’s Investor Service, Inc., or Standard & Poor’s Corporation. Eligible paper is further limited to issuing corporations that are organized and operating within the United States and have total assets in excess of five hundred million dollars (\$500,000,000.00) and having an “A” or higher rating for the issuer’s debt, other than commercial paper, if any, as provided for by Moody’s Investors Service, Inc., or Standard & Poor’s.
7. Corporation purchases of eligible commercial paper may not exceed 270 days maturity nor represent more than 10 percent of the outstanding paper of any issuing corporation. Purchases of commercial paper may not exceed 10 percent of the City’s surplus money that may be invested pursuant to this section. An additional 15 percent, or a total of 25 percent of the City’s surplus money, may be invested only if the dollar-weighted average maturity of the entire amount does not exceed 31 days.
8. Money Market Funds are eligible for investment if the companies providing the mutual funds invest only in instruments authorized by Government Code, Sections 53601 and/or 53635. In order to be an eligible money market investment under this section, the primary objective of the money market, as stated in the prospectus, is to maintain a constant \$1.00 Net Asset Value (NAV). The following additional guidelines include, but are not limited to:
  - The money market shall have attained the highest ranking or the highest letter and numerical rating provided by not less than two nationally recognized statistical rating organizations, and shall maintain these ratings for the duration of the investment.
  - Retain an investment advisor registered with the Securities and Exchange Commission (SEC) with not less than five (5) years’ experience investing in securities and obligations.
  - The fund shall have a minimum of \$500 million to total asset size of portfolio at time of investment, and should not drop below this threshold.
  - The purchase price of the share of beneficial interest shall not include any commission that these companies charge.
  - Purchases shall not exceed 15 percent of the City’s idle funds.

Summary of Maximum Percentage Limitations of Investments, by Investment Type

The following summary of maximum percentage limits, by instrument, is established for the City’s total pooled fund’s portfolio:

<u>Investment Type</u>	<u>Percentage</u>
U.S. Treasury Bills, Notes, and Bonds	0 to 100%
U.S. Government Agency Obligations	0 to 90%
Negotiable Certificates of Deposit	0 to 20%
Local Agency Investment Fund	\$50 million per account
Medium Term Corporate Notes	0 to 30%
Commercial Paper	0 to 10%
Money Market Funds	0 to 15%

**XI. Investment Pools**

Government sponsored investment pools (Pools) are permitted under California Government Code Section 53601 et seq. and an excellent short-term investment option for cash management facilities. These pools can provide safety, liquidity and yield in a single diversified investment. However, thoughtful investigation and due diligence are required both initially at the time of purchase and ongoing analysis to determine that the investment pool is being managed in a manner consistent with the objectives of the Policy.

State of California’s Local Agency Investment Fund (LAIF) is an example of a Pool. The City may invest in the LAIF established by the State Treasurer for the benefit of local agencies up to the maximum permitted by State law, but not to exceed 25% of the cost value (book value) of the total portfolio exclusive of the fiscal agent cash portfolio. Each agency is limited to an investment of \$50 million per account currently, but subject to change.

**XII. Collateralization**

Collateral for Certificates of Deposit (CD) and Negotiated Certificates of Deposit (NCD) must comply with Government Code, Chapter 4, Bank Deposit law Section 16500 et seq. and the Savings and Loan and Credit Union Deposit law Government Code Section 16600 et seq. In addition, if the CD is not FDIC insured or goes over the FDIC \$250,000 limit, collateral is required to equal 100 percent of the principal of either U.S. Treasury securities or Federal Agency securities.

Collateral will always be held by an independent third party with whom the City has a current custodial agreement. A clearly marked evidence of ownership (safekeeping receipt) must be supplied to the City and retained. The right of collateral substitution is granted, within the parameters and constraints of the Policy.

### **XIII. Safekeeping**

Securities purchased from broker/dealers shall be held in third party safekeeping by the trust department of the City's bank or other designated third party, in the City's name and control. The basic premise underlying the City's investment philosophy is and will continue to be to ensure that money is always safe and available when needed. All trades executed by a dealer will settle deliver vs. payment (DVP) through the City's safekeeping agent.

### **XIV. Performance Standards**

- A. The investment portfolio shall be designed with the objective of obtaining a rate of return throughout budgetary and economic cycles, commensurate with the investment risk constraints and the cash flow needs.
- B. The investment performance objective for the portfolio shall be to earn a total rate of return over a market cycle which is approximately equal to the return on a market benchmark Index of similar securities, as determined by the Director of Finance.
- C. Market Return (Benchmark): The City's investment strategy is active. Given this strategy, the basis used by the Director of Finance to determine whether market return is being achieved shall be to identify a benchmark which reflects a portfolio structure that is comparable to the City's portfolio. The City has chosen to use the Bank of America Merrill Lynch Index of 1 to 5 years Government securities.

### **XV. Diversification and Risk Tolerance**

The City of Richmond recognizes diversification is an investment strategy that will mitigate risk in the investment portfolio. Portfolio diversification is employed as a way to control risk. The City's investment portfolio shall be diversified to avoid incurring unreasonable and avoidable risks with regard to specific investment types. Within investment types, the City shall also maintain a mix of securities to avoid concentrations with individual financial institutions, geographic areas, industry types and maturities. No individual investment transaction shall be undertaken that jeopardizes the total capital position of the overall portfolio. The Treasurer shall periodically establish guidelines and strategies to control risks of default, market price changes, and illiquidity.

In addition to these general policy considerations, the following specific policies will be strictly observed:

- 1. All transactions will be executed on a delivery versus payment (DVP) basis.
- 2. A competitive bid process, when practical, will be used to place all investment purchases.

## **XVI. Interest Earnings**

All moneys earned and collected from investments authorized in this policy shall be allocated monthly to various fund accounts based on the cash balance in each fund as a percentage of the entire pooled portfolio. Should any fund not have a cash balance at the end of a month, it will receive none of the moneys earned and collected from the pooled investments. Furthermore, should any fund have a temporary negative cash balance at the end of a month, it will be charged for the use of the money at the aggregated earnings rate of the pooled investments.

## **XVII. Restrictions**

1. The City will not invest any funds in inverse floaters, range notes, or interest-only STRIPS (Separate Trading of Registered Interest and Principal of Securities) that are derived from a pool of mortgages.
2. The City will not invest any funds in any security that could result in zero interest accrual if held to maturity. This limitation does not apply to investments in shares of beneficial interest (money market mutual funds) that are authorized elsewhere in the Investment Policy.
3. It is the City's policy not to invest in companies involved in the manufacturing of tobacco and tobacco-related products such as cigarettes, cigars, pipe tobacco, chewing tobacco, etc.
4. In accordance with the Slavery Era Insurance Ordinance 14-05 N.S. Section 2.29.030 Social Disclosure on Gains from Slavery effective July 1, 2005, the City will not invest any funds in international financial instruments that benefited from slavery. The City Council prohibits, by social investment policy, such investments and reserves the absolute right to divest from such investments with the cost of divestment being borne by the contracting institution.

## GLOSSARY

**Agency bond:** Also known as Agency debt is a security, usually a bond, issued by United States (U.S.) government-sponsored agency. The offerings of these agencies are backed but not guaranteed by the U.S. government.

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

**Benchmark:** A comparative base for measuring the performance or risk tolerance of the investment portfolio. A benchmark should represent a close correlation to the level of risk and the average duration of the portfolio's investments.

**Bid:** The price offered by a buyer of securities. (When you are selling securities, you ask for a bid.) See Offer.

**Broker:** A broker brings buyers and sellers together for a commission.

**Certificate of deposit (CD):** A time deposit with a specific maturity evidenced by a Certificate. Large-denomination CD's are typically negotiable.

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

**Comprehensive Annual Financial Report (CAFR):** The official annual report for the government agency. It includes five combined statements for each individual fund and account group prepared in conformity with GAAP. It also includes supporting schedules necessary to demonstrate compliance with finance-related legal and contractual provisions, extensive introductory material, and a detailed Statistical Section.

**Dealer:** A dealer, as opposed to a broker, acts as a principal in all transactions, buying and selling for his own account.

**Delivery versus Payment (DVP):** There are two methods of delivery of securities: delivery versus payment and delivery versus receipt. Delivery versus payment is delivery of securities with an exchange of money for the securities. Delivery versus receipt is delivery of securities with an exchange of a signed receipt for the securities.

**Derivatives:** (1) Financial instruments whose return profile is linked to, or derived from, the movement of one or more underlying index or security, and may include a leveraging factor, or (2) financial contracts based upon notional amounts whose value is derived from an underlying index or security (interest rates, foreign exchange rates, equities or commodities).

**Discount:** The difference between the cost price of a security and its maturity when quoted at lower than face value. A security selling below original offering price shortly after sale also is considered to be at a discount.

**Diversification:** Investment contained within the portfolio will be diversified by security type, institution and maturity.

**Federal Credit Agencies:** Agencies of the Federal government set up to supply credit to various classes of institutions and individuals, e.g., saving and loan associations, small business firms, students, farmers, farm cooperatives, and exporters.

**Federal Deposit Insurance Corporation (FDIC):** A federal agency that insures bank deposits, currently up to \$100,000 per deposit.

**Federal Funds Rate:** The rate of interest at which Fed funds are traded. This rate is currently pegged by the Federal Reserve through open-market operations.

**Federal Home Loan Banks (FHLB):** Government sponsored wholesale banks (currently 12 regional banks), which lend funds and provide correspondent banking services to member commercial banks, thrift institutions, credit unions and insurance companies. The mission of the FHLBs is to liquefy the housing related assets of its members who must purchase stock in their district Bank.

**Federal National Mortgage Association (FNMA):** FNMA, like GNMA was chartered under the Federal National Mortgage Association Act in 1938. FNMA is a federal corporation working under the auspices of the Department of Housing and Urban Development (HUD). It is the largest single provider of residential mortgage funds in the United States. Fannie Mae, as the corporation is called, is a private stockholder-owned corporation. The corporation's purchases include a variety of adjustable mortgages and second loans, in addition to fixed-rate mortgages. FNMA's securities are also highly liquid and are widely accepted. FNMA assumes and guarantees that all security holders will receive timely payment of principal and interest.

**Federal Open Market Committee (FOMC):** Consists of seven members of the Federal Reserve Board and five of the twelve Federal Reserve Bank Presidents. The President of the New York Federal Reserve Bank is a permanent member, while the other Presidents serve on a rotating basis. The Committee periodically meets to set Federal Reserve guidelines regarding purchases and sales of Government Securities in the open market as a means of influencing the volume of bank credit and money.

**Federal Reserve System:** The central bank of the United States created by Congress and consisting of a seven member Board of Governors in Washington, D.C., 12 regional banks and about 5,700 commercial banks that are members of the system.

**Government National Mortgage Association (GNMA or Ginnie Mae):** Securities influencing the volume of bank credit guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loan associations, and other institutions. The security holder is protected by full faith and credit of the U.S. Government. Ginnie Mae securities are backed by the FHA, VA or FHA mortgages. The term "pass-throughs" is often used to describe Ginnie Maes.

**Liquidity:** A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value. In the money market, a security is said to be liquid if the spread between bid and asked prices is narrow and reasonable size can be done at those quotes.

**Local Government Investment Pool (LGIP):** The aggregate of all funds from political subdivisions that are placed in the custody of the State Treasurer for investment and reinvestment.

**Market Value:** The price at which a security is trading and could presumably be purchased or sold.

**Maturity:** The date upon which the principal or stated value of an investment becomes due and payable.

**Money Market:** The market in which short-term debt instruments (bills, commercial paper, bankers' acceptances, etc.) are issued and traded.

**Offer:** The price asked by a seller of securities. (When you are buying securities, you ask for an offer.) See Bid.

**Open Market Operations:** Purchases and sales of government and certain other securities in the open market by the New York Federal Reserve Bank as directed by the FOMC in order to influence the volume of money and credit in the economy. Purchases inject reserves into the bank system and stimulate growth of money and credit; sales have the opposite effect. Open market operations are the Federal Reserve's most important and most flexible monetary policy tool.

**Portfolio:** Collection of securities held by an investor.

**Primary Dealer:** A group of government securities dealers who submit daily reports of market activity and positions and monthly financial statements to the Federal Reserve Bank of New York and are subject to its informal oversight. Primary dealers include Securities and Exchange Commission (SEC)-registered securities broker-dealers, banks, and a few unregulated firms.

**Prudent Person Rule:** An investment standard. In some states the law requires that a fiduciary, such as a trustee, may invest money only in a list of securities selected by the custody state—the so-called legal list. In other states the trustee may invest in a security if it is one which would be bought by a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital.

**Rate of Return:** The yield obtainable on a security based on its purchase price or its current market price. This interest may be amortized yield to maturity on a bond or the current income return.

**Safekeeping:** A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank's vaults for protection.

**Secondary Market:** A market made for the purchase and sale of outstanding issues following the initial distribution.

**Securities & Exchange Commission:** Agency created by Congress to protect investors in securities transactions by administering securities legislation.

**Securities and Exchange Commission (SEC) Rule 15C3-1:** See Uniform Net Capital Rule.

**Structured Notes:** Notes issued by Government Sponsored Enterprises (FHLB, FNMA, SLMA, etc.) and Corporations, which have imbedded options (e.g., call features, step-up coupons, floating rate coupons, and derivative-based returns) into their debt structure. Their market performance is impacted by the fluctuation of interest rates, the volatility of the imbedded options and shifts in the shape of the yield curve.

**Treasury Bills:** A non-interest bearing discount security issued by the U.S. Treasury to finance the national debt. Most bills are issued to mature in three months, six months, or one year.

**Treasury Bonds:** Long-term coupon-bearing U.S. Treasury securities issued as direct obligations of the U.S. Government and having initial maturities of more than 10 years.

**Treasury Notes:** Medium-term coupon-bearing U.S. Treasury securities issued as direct obligations of the U.S. Government and having initial maturities from two to 10 years.

**Uniform Net Capital Rule:** Securities and Exchange Commission requirement that member firms as well as nonmember broker-dealers in securities maintain a maximum ratio of indebtedness to liquid capital of 15 to 1; also called net capital rule and net capital ratio. Indebtedness covers all money owed to a firm, including margin loans and commitments to purchase securities, one reason new public issues are spread among members of underwriting syndicates. Liquid capital includes cash and assets easily converted into cash.

**Yield:** The rate of annual income return on an investment, expressed as a percentage. (a) Income Yield is obtained by dividing the current dollar income by the current market price for the security. (b) Net Yield or Yield to Maturity is the current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond.

## **APPENDIX B**

### **City of Richmond Post-Issuance Tax Compliance Procedures For Tax-Exempt and Build America Bonds**

The purpose of these Post-Issuance Tax Compliance Procedures is to establish policies and procedures in connection with tax-exempt bonds and “Build America Bonds” (“Bonds”) issued by the City of Richmond, the Richmond Joint Powers Authority, the Richmond Community Redevelopment Agency, and RHA Properties (together, the “City”) so as to ensure that the City complies with all applicable post-issuance requirements of federal income tax law needed to preserve the tax-exempt or build America bond status of the Bonds.

#### **General**

Ultimate responsibility for all matters relating to City financings and re-financings [other than Tax and Revenue Anticipation Notes (“TRANs”)] rests with the Finance Director/Treasurer.

#### **Post-Issuance Compliance Requirements**

##### External Advisors / Documentation

The Finance Director and other appropriate City personnel shall consult with bond counsel and other legal counsel and advisors, as needed, throughout the Bond issuance process to identify requirements and to establish procedures necessary or appropriate so that the Bonds will continue to qualify for the appropriate tax status. Those requirements and procedures shall be documented in a City resolution(s), Tax Certificate(s) and / or other documents finalized at or before issuance of the Bonds. Those requirements and procedures shall include future compliance with applicable arbitrage rebate requirements and all other applicable post-issuance requirements of federal tax law throughout (and in some cases beyond) the term of the Bonds.

The Finance Director and other appropriate City personnel also shall consult with bond counsel and other legal counsel and advisors, as needed, following issuance of the Bonds to ensure that all applicable post-issuance requirements in fact are met. This shall include, without limitation, consultation in connection with future contracts with respect to the use of Bond-financed assets and future contracts with respect to the use of output or throughput of Bond-financed assets.

Whenever necessary or appropriate, the City shall engage expert advisors (each a “Rebate Service Provider”) to assist in the calculation of arbitrage rebate payable in respect of the investment of Bond proceeds.

#### Role of the City as Bond Issuer

Unless otherwise provided by City resolutions, unexpended Bond proceeds shall be held by the Trustee, and the investment of Bond proceeds shall be managed by the Finance Director. The Trustee shall maintain records and shall prepare regular, periodic statements to the City regarding the investments and transactions involving Bond proceeds.

#### Arbitrage Rebate and Yield

Unless a Tax Certificate documents that bond counsel has advised that arbitrage rebate will not be applicable to an issue of Bonds:

- the City shall engage the services of a Rebate Service Provider, and the City or the Bond trustee shall deliver periodic statements concerning the investment of Bond proceeds to the Rebate Service Provider on a prompt basis;
- upon request, the Finance Director and other appropriate City personnel shall provide to the Rebate Service Provider additional documents and information reasonably requested by the Rebate Service Provider;
- the Finance Director and other appropriate City personnel shall monitor efforts of the Rebate Service Provider and assure payment of required rebate amounts, if any, no later than 60 days after each 5-year anniversary of the issue date of the Bonds, and no later than 60 days after the last Bond of each issue is redeemed; and
- during the construction period of each capital project financed in whole or in part by Bonds, the Finance Director and other appropriate City personnel shall monitor the investment and expenditure of Bond proceeds and shall consult with the Rebate Service Provider to determine compliance with any applicable exceptions from the arbitrage rebate requirements during each 6-month spending period up to 6 months, 18 months or 24 months, as applicable, following the issue date of the Bonds.

The City shall retain copies of all arbitrage reports and trustee statements as described below under “Record Keeping Requirements”.

#### Use of Bond Proceeds

The Finance Director and other appropriate City personnel shall:

- monitor the use of Bond proceeds, the use of Bond-financed assets (e.g., facilities, furnishings or equipment) and the use of output or throughput of Bond-financed assets

throughout the term of the Bonds (and in some cases beyond the term of the Bonds) to ensure compliance with covenants and restrictions set forth in applicable County resolutions and Tax Certificates;

- maintain records identifying the assets or portion of assets that are financed or refinanced with proceeds of each issue of Bonds;
- consult with Bond Counsel and other professional expert advisers in the review of any contracts or arrangements involving use of Bond-financed facilities to ensure compliance with all covenants and restrictions set forth in applicable City resolutions and Tax Certificates;
- maintain records for any contracts or arrangements involving the use of Bond-financed facilities as might be necessary or appropriate to document compliance with all covenants and restrictions set forth in applicable City resolutions and Tax Certificates;
- meet at least annually with personnel responsible for Bond-financed assets to identify and discuss any existing or planned use of Bond-financed, assets or output or throughput of Bond-financed assets, to ensure that those uses are consistent with all covenants and restrictions set forth in applicable City resolutions and Tax Certificates.

All relevant records and contracts shall be maintained as described below.

#### Record Keeping Requirements

Unless otherwise specified in applicable City resolutions or Tax Certificates, the City shall maintain the following documents for the term of each issue of Bonds (including refunding Bonds, if any) plus at least three years:

- a copy of the Bond closing transcript(s) and other relevant documentation delivered to the City at or in connection with closing of the issue of Bonds;
- a copy of all material documents relating to capital expenditures financed or refinanced by Bond proceeds, including (without limitation) construction contracts, purchase orders, invoices, trustee requisitions and payment records, as well as documents relating to costs reimbursed with Bond proceeds and records identifying the assets or portion of assets that are financed or refinanced with Bond proceeds;
- a copy of all contracts and arrangements involving private use of Bond-financed assets or for the private use of output or throughput of Bond-financed assets; and
- copies of all records of investments, investment agreements, arbitrage reports and underlying documents, including trustee statements.

**Interest Rate Swap Policy of the City of Richmond  
Established by the Finance Department**

***Fiscal Year 2016-17***

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**Scope and Authority**

*This Interest Rate Swap Policy (the Policy), established by and for the Finance Department, is designed to provide procedural direction to the City of Richmond Finance Department, the Richmond Housing Authority, the Richmond Community Redevelopment Agency, the Richmond Joint Powers Finance Authority and the City itself regarding the utilization, execution, and management of interest rate swaps and related instruments (collectively, “interest rate swaps”). While adherence to this Policy is required in applicable circumstances, it is recognized that changes in the capital markets, agency programs, and other unforeseen circumstances may from time to time produce situations that are not covered by this Policy, and will require modifications or exceptions to achieve policy goals. In these cases, management flexibility is appropriate. Periodically, but at least annually, the City will review the Policy and shall make modifications as appropriate due to changes in the business environments or market conditions.*

*The City of Richmond is authorized under California Government Code Section 5922 to enter into interest rate swaps to reduce the amount and duration of rate, spread, or similar risk when used in combination with the issuance of bonds.*

*This Policy and any subsequent amendments hereto shall be on file with Finance Department, contained on the City’s website, with copies delivered to the City Clerk, the City Council and the Chair of the Finance Committee of the City Council.*

**Mission of the Finance Department Treasury Division**

Issue and manage short and long-term financings (bonds, TRANs, etc), both for capital improvement and operating needs, by balancing market and credit risk with satisfactory economic benefits and proper fiscal controls.

**I. Interest Rate Swap Objectives**

- Reduce or manage exposure to changes in interest rates on a particular financial transaction or in the context of the management of interest rate risk derived from the City’s overall asset/liability balance consistent with prudent debt and risk guidelines.
- Result in a lower net cost of borrowing with respect to the City’s debt or achieve a higher net rate of return on investments made in connection with, or incidental to the issuance, or carrying of the City’s debt obligations or other City investments.
- Manage variable interest rate exposure consistent with prudent debt practices.

- Enhance investment returns within prudent risk guidelines.
- Manage exposure to changing market conditions in advance of anticipated bond issues (through the use of anticipatory hedging instruments).
- Achieve more flexibility in meeting overall financial objectives than can be achieved in conventional markets.

## **II. Permitted Instruments**

The City may utilize the following financial products on a current, or forward basis, after identifying the objectives to be realized and assessing the attendant risks.

- Interest rate swaps, including (i) pay fixed/receive floating swaps (fixed rate swaps), (ii) receive floating/pay fixed swaps (floating rate swaps) and (iii) pay floating/receive floating swaps (basis swaps). Swaps may include option features, such as for the extension, cancellation, or index conversion of the swap.
- Interest rate caps, floors, and collars.
- Stand-alone options to enter into swaps (swaptions) on a particular date, series of dates, or during a particular period of time in the future.

## **III. Conditions for the Use of Interest Rate Swaps**

Each Agreement and Transaction will be entered into not for purpose of speculation, but solely in connection with the financing activities of the City.

- A. General Usage** Interest rate swaps may be used to lock-in a fixed rate or, alternatively, to create additional variable rate exposure. Interest rate swaps may be used to produce interest rate savings, limit or hedge variable rate payments, alter the pattern of debt service payments, or for asset/liability matching purposes.
- B. Liquidity Considerations** The impact on the cost and availability of letters of credit and liquidity support for both new and existing variable rate programs shall be considered when evaluating the issuance of new variable rate bonds which are to be swapped to a fixed rate liquidity support. Due to the limited supply of letter of credit or liquidity facility support in connection with variable rate bonds, higher overall costs may result.
- C. Call Option Value Considerations** When considering the relative advantage of a fixed rate swap to fixed rate bonds, the value of the call option that would typically be purchased for the fixed rate bonds shall be compared to the incremental present value of the savings from using a swap. This shall be done to ensure the benefit from use of the swap will provide sufficient compensation to offset the expected value of any foregone future refunding savings.

#### **IV. Interest Rate Swap Features**

**A. Interest Rate Swap Agreement** Each interest rate swap executed by the City shall contain terms and conditions as set forth in an International Swaps and Derivatives Association, Inc. (ISDA) Master Agreement, including any Schedules to the Master Agreement, Confirmations and Credit Support Annexes, or other comparable agreement widely used by recognized derivatives dealers. The swap agreements between the City and each qualified swap Counterparty shall include payment, term, security, collateral, default, remedy, termination, and other terms, conditions and provisions as the Finance Director deems necessary or desirable.

The City may use law firms and financial advisory firm(s) with recognized experience in derivatives transactions to assist in preparation of the swap documents.

**B. Interest Rate Swap Counterparties** The City will do business only with qualified swap counterparties. Qualified counterparties are institutions whose long-term credit rating or whose obligations are guaranteed by a financial institution whose long term credit rating are at the time the swap is entered into at least as high as “A” or “A2” or equivalent and that have a demonstrated record of successfully executing swap transactions. The City will structure interest rate swap agreements to protect itself from credit deterioration of counterparties, including the use of ratings-based termination events, credit support annexes or other forms of credit enhancement. Such protection shall include any terms and conditions which the City deems necessary or appropriate to protect its interests.

**C. Term and Notional Amount** The City shall determine the appropriate term and size for an interest rate swap agreement on a case-by-case basis. In connection with the issuance or carrying of bonds, the outstanding notional amount of a swap agreement should relate to the amortization of the related existing or anticipated debt of the City. While entering into a swap with a term less than the associated bonds may be appropriate, if the intent is to “rollover” the swap, the City will be subject to the uncertainties of entering into a new swap at then prevailing market conditions.

**D. Collateral Requirements** Terms imposing collateral requirements based on credit ratings of the counterparty, requiring collateralization or other forms of credit enhancements to secure any or all swap payment obligations may be included as part of any swap agreement. The collateral requirements will be determined in consultation with counsel and the financial advisor and/or swap advisor, and may require the counterparty to post securities, surety bonds, letters of credit or other credit enhancement if the highest credit rating of the counterparty, its parent, or guarantor is or falls below a rating of “AA-“ or “Aa3”. Additional collateral for further decreases in credit ratings of each counterparty shall be posted in accordance with the provisions contained in the CSA or other collateral support agreement of the Agreement.

Threshold collateral amounts shall be determined on a case-by-case basis. Reasonable threshold limits will be established for the initial deposit and for increments of collateral posting thereafter. Collateral shall be deposited with a third party trustee or as mutually agreed upon between the City and the counterparty. A list of acceptable securities that may be posted as collateral and the valuation of such collateral will be determined and mutually agreed upon during negotiation of the swap agreement with each swap counterparty. The market value of the collateral shall be determined on a monthly basis, or more frequently if the City determines it is in its best interest given the specific nature of the swap(s) and/or collateral security.

**E. Security and Source of Repayment** Generally, the same security and source of repayment (pledged revenues) will secure the interest rate swaps as is used to secure the bonds that are hedged or carried by the swap, if any. The costs and benefits of subordinating the payments under the swap and/or termination payment shall be considered.

**F. Cancellation Provisions** The benefit of purchasing the right to cancel the interest rate swap at no cost (par call) after a specified period of time, generally 5 to 10 years shall be evaluated. If the cancellation option is cost efficient relative to the cost of obtaining a bond call option for a similar starting period, it will be purchased. A par call termination provision mitigates some risks of the swap, by allowing a no-cost termination any time after the exercise date.

**G. Prohibited Interest Rate Swap Features** The City will not use interest rate swaps that (i) are speculative or create extraordinary leverage or risk, (ii) lack adequate liquidity to terminate without incurring a significant bid/ask spread, (iii) provide insufficient price transparency to allow reasonable valuation, or (iv) are used as investments.

## **V. Evaluation of Proposed Transactions**

The City's staff shall undertake an evaluation of any proposed transaction. This will include, but not be limited to, consideration of the following:

- Assessment of all inherent risks of the transaction including, but not limited to those outlined below (see **Interest Rate Swap Risks**)
- Alternative financing options and a comprehensive evaluation of the potential risks and expected benefits of the interest rate swap relative to such other options.

- Security and source of payments, for both scheduled and termination payments, and the integration of the swap into the City's debt program.
- Procurement process and the suitability of the contemplated counterparties to the swap, taking into account any existing exposure to such counterparties.
- Impact on City's credit and liquidity profile and how other financial arrangements, existing or expected, may be impacted by the swap.
- Analysis of impact on the City's net variable rate interest exposure from the contemplated transaction and any potential budgetary impact.
- Cost and availability of on-going resources for the effective operations and risk management of the swap.
- Tax, accounting, or other compliance requirements relative to other options.
- If the transaction includes option components, analysis of circumstances under which the option will likely, or not likely, be exercised and the consequences of each outcome.
- Volatility Exposure (as outlined herein) for each counterparty for all existing and any proposed transactions.

## **VI. Interest Rate Swap Risks**

Before proceeding with a swap transaction, the City must reasonably conclude that the expected benefits of the transaction outweigh the expected risks, that the risks are within acceptable levels, and that the contemplated transaction does not impose risks that threaten the City's ability to perform its core functions. The transaction must be reasonable in relation to the City's overall financial condition and capitalization.

The City shall, with its advisors and legal counsel, structure swap transactions with terms and provisions that will help mitigate such risks to the extent practicable and cost-effective. The City shall have a plan for the on-going monitoring and risk management of swap transactions.

- A. Counterparty Risk** The failure of the counterparty to make required payments or otherwise comply with the terms of the swap agreement. If the swap is terminated prior to its scheduled final cash flow date and the City's swap position has increased in value, the City will be owed a termination amount and therefore will have credit exposure to its counterparty for collection of any such amount.
  - 1. Assessment** The City will monitor counterparty exposure levels, ratings thresholds, and collateralization requirements.
- B. Termination Risk** The risk that an interest rate swap agreement must be terminated prior to its stated final cash flow date, and that the City cannot obtain a replacement transaction with substantially similar term, including because of deterioration of the City's own credit. In such a circumstance, the City could owe, or be owed, a termination payment.

**1. Assessment** The City will compute, at least annually, the termination exposure for all existing and proposed swaps at market value and under an expected worse-case scenario. A contingency plan will be annually updated specifying to finance a termination payment and/or replace the hedge.

**C. Collateral Posting Risk** The risk that the City will be required to secure its payment obligations under the swap. Posted collateral would not be available for the City's expenditure or reserve balance needs, potentially adversely impacting credit ratings and overall liquidity and budgetary efforts.

**1. Assessment** The City will review, on a case by case basis, the possible risk associated with posting collateral, taking into consideration any earnings potential on posted collateral.

**D. Basis Risk** The risk of a mismatch between actual variable rate debt service and variable rate indices used to determine swap payments.

**1. Assessment** On an annual basis the City will review historical trading differentials between the variable rate bonds and the indices.

**E. Tax Risk** The risk created by potential tax events that could affect sufficiency of swap payments.

**1. Assessment** The City will review all tax events in proposed swap agreements and evaluate the impact of potential changes in tax law on LIBOR indexed swaps.

**F. Rollover Risk** The risk of a mismatch of the maturity of the swap and the maturity of the underlying bonds.

**1. Assessment** The City will determine, in accordance with its Debt Policy, the capacity to issue variable rate bonds that may be outstanding after the maturity of a fixed rate swap.

**G. Liquidity Risk** In connection with a swap strategy which includes issuance of floating rate bonds that, absent the swap strategy would have been issued as fixed rate bonds, the risk that the City cannot secure a cost-effective renewal of a letter or line of credit or suffers a failed auction or remarketing with respect to the floating-rate bonds.

**1. Assessment** The City will evaluate the expected availability of liquidity support for hedged (swapped) and non-swapped variable rate debt.

**H. Credit Risk** The risk of an event occurring that modifies the credit quality or credit rating of the issuer of its counterparty.

**1. Assessment** The City will monitor the ratings of counterparties, insurers, and guarantors.

**VII. Counterparty Credit Exposure**

The City will manage its counterparty credit exposure (i.e., amounts which would become due to the City if the swaps with a particular counterparty were to terminate early pursuant to a default or other similar event) through diversification and active trade management. In order to manage the City’s exposure, the City shall annually calculate and review the current market evaluation of all outstanding swaps, subtotaled by counterparty and by security and source of payment (as applicable). In addition, for each counterparty, the City will review the then current long-term credit ratings and the ratings outlook, including the date of the last rating update. The calculation of termination exposure per counterparty will be on a net basis by taking into consideration multiple transactions, some of which may offset the overall exposure to the City.

In addition, the City shall annually estimate the interest rate volatility risk (“Volatility Exposure”) of the City’s swap portfolio. The purpose of the Volatility Exposure is to measure what impact a significant change in interest rates would have on the City’s swap portfolio. Volatility Exposure will be calculated assuming (i) an upward shift of 150 basis points in the yield curve and (ii) a downward shift of 150 basis points in the yield curve. The assumed shift will be reviewed periodically to ensure that they remain appropriate.

**Example of Counterparty Credit Exposure Information (Illustration Purposes Only)**

<b>Counterparty</b>	<b>S&amp;P (Date) Moody’s (Date)</b>	<b>Outlook</b>	<b>Market Value of Transactions</b>	<b>Volatility Exposures Market Value</b>
<b>Provider A</b>	<b>A+ (1/1/04) A2 (1/1/05)</b>	<b>Stable Negative</b>	<b>\$3 million</b>	<b>VolExp<sub>Up</sub> \$4 million VolExp<sub>Down</sub> -\$1 million</b>

**A. Exposure Review of Existing Swaps** While collateralization reduces credit risk, collateralization introduces other risks, principally legal and operational. In order to manage these other risks, the City shall limit the amount of exposure to any one counterparty, regardless of the counterparty credit ratings and threshold levels. Credit exposure may be reduced, for example, through a swap termination, in whole or in part, or a restructuring of the swap to an on-market rate with a smaller notional amount accompanied by a cash payment to the City, which could then be used to redeem underlying debt obligations. These counterparty credit risk guidelines will not mandate or otherwise force automatic termination by the City or the counterparty.

**B. Exposure Review of Proposed Swaps** Prior to entering into a new swap transaction, the City, as part of its evaluation of the proposed transaction, will compute the Volatility Exposure by treating the proposed swap transaction as an outstanding swap. Such provisions will act only as guidelines in making a determination as to whether or not a proposed transaction should be executed given certain levels of existing and projected net termination exposure to a specific counterparty. These guidelines are not intended to require retroactively additional collateral posting for existing transactions.

## **VIII. Ongoing Risk Management and Reporting Requirements**

**A. Active Management** The City will seek to maximize the benefits and minimize the risks it carries by actively managing its interest rate swap program. This will entail monitoring the adequacy of posted collateral, compliance with accounting requirements, and periodic monitoring of market conditions for emergent opportunities and risks. Active management may require modifications of existing positions including, for example:

- Early Termination;
- Shortening or lengthening the term;
- Sale or purchase of options;
- Basis conversion

**B. On-going Reporting** A report providing the status of all interest rate swap agreements entered into by the City will be prepared no less frequently than annually and shall include the following:

- A description of all outstanding interest rate swap agreements, including project and bonds series, type of swap, rates paid and received by the City, total notional amount, average life of each swap agreement, and remaining term of each swap agreement.
- Highlights of all material changes to swap agreements or new swap agreements entered into by the City since the immediately preceding report.
- Market value of each of the City's interest rate swap agreements.
- The credit rating of each swap counterparty and credit enhancer insuring swap payments, if any.
- Listing of any credit enhancement, liquidity facility or reserves and accounting of all costs and expenses associated with the credit enhancement, liquidity facility or reserves.
- The mark to market value for each transaction and the aggregate for each counterparty.

**Reserve Policy of the City of Richmond  
Established by the Finance  
Department Fiscal Year 2016-17**

**Policy Guidelines**

Municipal governments provide a wide range of services that have an impact on public safety and quality of life for community members. Prudent use of resources helps determine how effectively these services are provided on an ongoing basis. In addition to managing revenues and expenditures, it is also the municipal finance official's responsibility to focus on the General Fund balance and cash reserves.

The City shall maintain year end contingency reserve balances in the General Fund, including PERS savings reserves but excluding departmental carryover, of minimum 7 % of the next year's budgeted General Fund expenditures. This is the minimum needed to maintain the City's creditworthiness and to adequately provide for economic and legislative uncertainties, cash flow needs and contingencies. City Council approval is required before any withdrawals from the reserve fund. The Council shall have the discretion to use the reserve for one time emergencies only and not to be used for ongoing expenses. As the City experiences net revenue gains in future years, the reserve balance must grow back to 7% of total expenditures, following the stabilization policy, in order to allow the City to build up its capacity to handle future short term economic downturns or emergencies without cutting services.

A policy based upon a percentage assures that the reserve will remain a prudent cushion as the City's budgets grow over time.

**Pension Stabilization Fund**

As covenanted by the City, the Trustee for the 2005 pension obligation bonds has established a special fund called the "Pension Stabilization Fund". On or before June 30 of each fiscal year, commencing in Fiscal Year 2005-06, the City shall deposit into the Pension Stabilization Fund the amounts as set forth in the Indenture of the 2005 Pension Obligation Bonds which represent the amount by which the total amount of principal and interest on the Series 2005 Bonds for such fiscal year is less than the amount which would have been paid with respect to PERS Obligation had the Series 2005 Bonds not been issued. The Pension Stabilization Fund is funded from the savings achieved from issuing the 2005 Pension Funding Bonds. As described in the Trust Indenture of the 2005 Pension Obligation Bonds, these funds can be used for the following purposes:

- § Pay Principal, Accreted Value of or Interest on 2005 Pension Obligation Bonds
  
- § Transfer to City for payment of
  - § Pension costs of the City's CalPERS pension programs
  - § Capital project costs
  - § Retiree health care costs