



Agenda Item No. (9)

To: Finance-Auditing Committee/Committee of the Whole
Meeting of February 25, 2021

From: Alice Ng, Director of Fiscal Resources
Joseph M. Wire, Auditor-Controller
Denis J. Mulligan, General Manager

Subject: **APPROVE ACTIONS RELATIVE TO THE ANNUAL REVIEW OF RULE XI, INVESTMENT POLICY, OF THE RULES OF THE BOARD**

Recommendation

The Finance-Auditing Committee recommends that the Board of Directors approve the following actions relative to the annual review of RULE XI, **INVESTMENT POLICY**, of the *Rules of the Board*:

1. Renew the annual delegation of investment management authority to the Auditor-Controller for FY 21/22 as per RULE XI, **INVESTMENT POLICY**, **Section E, Delegation of Authority**, of the *Rules of the Board*, and as provided for in California Government Code Section 53607.
2. Approve an amendment to RULE XI, **INVESTMENT POLICY**, of the *Rules of the Board* as set forth below.

This matter will be presented to the Board of Directors at its February 26, 2021, meeting for appropriate action.

Summary

Renew Delegation of Investment Management Authority to Auditor-Controller

In accordance with Section E of RULE XI, **INVESTMENT POLICY**, of the *Rules of the Board*, the delegation of investment management authority by the Board to the Auditor-Controller is for a one-year period and is subject to annual Board review and renewal, as provided for in California Government Code Section 53607.

Staff recommends that the Finance-Auditing Committee recommend that the Board of Directors renew the annual delegation of investment management authority to the Auditor-Controller for FY 21/22.

Amendment to Investment Policy

Based on the Annual Investment Policy Review Memo (enclosed as Attachment 1) produced by the District's investment advisor, PFM Asset Management LLC, ("PFM"), and reviewed by District Counsel, staff recommends that certain sections of RULE XI, **INVESTMENT POLICY**, of the *Rules of the Board* be amended to improve clarity and to bring the Policy up-to-date with recent changes to the California Government Code. These recommendations are noted in the redlined Policy enclosed as Attachment 2 and summarized as follows:

Section G. Internal Controls

To clarify when the independent auditor will conduct their review, staff recommends adding the phrase "annually during the external financial statement audit" to the sentence relating to the independent auditor's review of the District's internal controls.

Section I. Permitted Investments

Staff recommends adding a new subsection titled "**Reverse Purchase Agreements**" before the last paragraph in subsection **1. Repurchase Agreements** to more clearly delineate which additional restrictions apply to repurchase agreements and which apply to reverse repurchase agreements.

Section M. Ineligible Investments

Staff recommends revising language to this section to improve clarity and to include an updated list of investments prohibited by Government Code Section 53601.6, which was recently amended by Senate Bill 998. These changes are explained in more detail in PFM's memo attached.

Section Q. Investment Sub-Committee

Staff recommends revising the language to clarify that the Investment Sub-Committee shall be established periodically, as needed.

Fiscal Impact

There is no fiscal impact associated with this report.

Attachments: Attachment 1 - PFM Annual Investment Policy Review Memo
Attachment 2 - Rule XI. Investment Policy (Redlined)



February 10, 2021

Memorandum

To: Joseph M. Wire, Auditor-Controller
Alice Ng, Director of Fiscal Resources
Golden Gate Bridge, Highway & Transportation District

From: Lesley Murphy, Senior Managing Consultant
PFM Asset Management LLC

Re: Annual Investment Policy Review

We have completed our annual review of the Investment Policy (the “Policy”) for the Golden Gate Bridge, Highway & Transportation District (the “District”). The Policy remains in compliance with all applicable California Government Code (Code) statutes regulating the investment of public funds. This year, our proposed changes to the Policy are largely minor and are designed to reflect recent updates to Code and/or to provide additional clarity to the Policy.

Additionally, we want to make the District aware of several recent changes to the sections of California Government Code that govern the investment of public agency funds.

We have also included a redlined version of the Policy with our proposed modifications.

General Recommended Modifications

I. Permitted Investment Instruments

We recommend adding the sub-heading **2. Reverse Repurchase Agreements** to more clearly delineate which additional restrictions apply to repurchase agreements and which apply to reverse repurchase agreements.

M. Ineligible Investments

In the first bullet, we recommend that the District strike the language related to “complex” security types, as this terminology may be misleading and ambiguous. Instead, we recommend that the language in this section clearly focus on some of the types of securities that are prohibited. We are also recommending a change to the second bullet in this section, as described in more detail below.



Information and Recommended Modifications Related to Code Changes

Senate Bill 998 – Overview

Senate Bill 998 (“SB 998”), which took effect on January 1, 2021 and shall be in effect until January 1, 2026, made a number of amendments to certain sections of the Code which govern the investment of public funds. Below we have included a summary of these amendments along with our recommendations for the District’s Policy. We note that the District’s Policy references certain sections of Code, rather than repeating these sections of Code verbatim; thus, in several instances, the amendments to Code do not necessitate changes to the District’s Policy. The amendments to Code include:

1. Allowing investment in securities issued or backed by the U.S. government that could result in zero or negative interest accrual if held to maturity, in the event of, and for the duration of, a period of negative market interest rates;

Recommendation: We recommend that the District amend the second bullet of M. Ineligible Investments to reflect the fact that public agencies are now permitted to invest in zero- or negative-interest accrual securities, under certain circumstances, and provided that the securities are issued by, or backed by, the United States government.

2. Deleting the commercial paper language regarding the issuing corporation’s outstanding paper;

Recommendation: No Policy changes necessary.

3. Establishing a 10% issuer limit on commercial paper and corporate notes for all agencies, other than a county or a city and a county;

Recommendation: No Policy changes necessary; we note that the Policy already establishes a more stringent 5% per issuer limit across all credit-sensitive security types.

4. Allowing local agencies that have more than \$100 million of investment assets under management to invest up to 40% in commercial paper (existing limit is 25% for all agencies, other than a county or a city and county); and

Recommendation: No Policy changes necessary.



5. Adding permission for federally recognized Indian tribes to invest and participate in investment JPAs.

Recommendation: No Policy changes necessary.

We look forward to further discussing these recommendations with you. Please let us know if you have any questions.

THIS PAGE INTENTIONALLY LEFT BLANK

RULES XI. INVESTMENT POLICY

A. Introduction

The purpose of this Rule is to identify various policies and procedures that enhance opportunities for a prudent and systematic investment policy and to organize and formalize investment-related activities.

The investment policies and practices of the Golden Gate Bridge, Highway & Transportation District are based on state law and prudent money management. All general funds will be invested in accordance with the District's Investment Policy and shall be consistent with the provisions of Articles 1 and 2 of Chapter 4 of the California Government Code (commencing with Section 53600). The investment of bond or note proceeds will be governed by the provisions of the relevant bond documents. (Res. 01-148, 9/14/01; Res. 2011-047, 5/27/11; Res. 2012-044, 6/22/12.)

B. Scope

It is intended that this policy cover all funds (except retirement funds) and investment activities under the direction of the District.

C. Prudence

Investments shall be made with judgment and care—under circumstances then prevailing—which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

The standard of prudence to be used by investment officials shall be the “prudent investor” standard and shall be applied in the context of managing an overall portfolio. All persons investing, reinvesting, purchasing, acquiring, exchanging, selling and managing public funds shall act with care, skill, prudence and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and anticipated needs of the District, 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 District. (Res. 2011-047, 5/27/11.)

D. Objectives

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

1. Safety. Safety of principal is the foremost objective of the investment program. The District's investments shall be undertaken in a manner that seeks to ensure preservation of capital in the portfolio.

2. Liquidity. The District's investment portfolio will remain sufficiently liquid to enable the District to meet its cash flow requirements.

3. Return On Investment. The District's investment portfolio shall be designed with the objective of attaining a market rate of return on its investments consistent with the constraints imposed by its safety objective and cash flow considerations.

E. Delegation of Authority

The management and oversight responsibility for the Investment Program is hereby delegated for a one-year period to the Auditor-Controller who shall monitor and review all investments for consistency with this Investment Policy and provide monthly reports of investment transactions to the Board. The Board shall review, and may renew the delegation of authority to the Auditor-Controller on an annual basis. (Res. 2017-023, 2/24/17.) No person may engage in an investment transaction except as provided under the limits of this policy. The Board may delegate the day-to-day investment decision making and execution authority to an investment advisor. The advisor shall follow the policy and such other written instructions as are provided. (Res. 2011-047, 5/27/11.)

F. Ethics and Conflict of Interest

Officers and employees involved in the investment process shall refrain from personal business activities that could conflict with proper execution of the investment program, or which could impair their ability to make impartial decisions. Officers and employees involved in the investment process shall abide by the District's Conflict of Interest Code, California Government Code Section 1090 et seq. and the California Political Reform Act (California Government Code Section 81000 et seq.)

G. Internal Controls

The Auditor-Controller shall establish a set of internal controls. The internal controls will be reviewed with the independent auditor annually during the external financial statement audit. The controls shall be designed to prevent employee error, misrepresentations by third parties, unanticipated changes in financial markets or imprudent actions by employees or officers of the District.

H. Selection of Financial Institutions and Broker/Dealers

To provide for the optimum yield in the District's portfolio, the District's procedures shall be designed to encourage multiple bids and offers on investment transactions from an approved list of broker/dealers. The Auditor-Controller, or the District's investment advisor, shall maintain a list of authorized broker/dealers and financial institutions which are approved for investment purposes, and it shall be the policy of the District to purchase securities only from those authorized institutions or firms.

I. Permitted Investment Instruments

California Government Code Section 53601 (Section 53601) sets forth the securities that public agencies, such as the District, are permitted to invest in. The Board of Directors authorizes the investment of District funds in the categories of securities authorized by Section 53601, as it may be amended from time to time, subject to the following additional restrictions:

1. Repurchase Agreements

Repurchase agreements may be used solely as short-term investments not to exceed 90 days.

Only U.S. Treasury securities or Federal Agency securities, as defined in the subdivisions of Section 53601, will be acceptable collateral.

Market value must be calculated each time there is a substitution of collateral.

The District or its trustee shall have a perfected first security interest under the Uniform Commercial Code in all securities subject to repurchase agreement.

The District may enter into repurchase agreements only with primary dealers of the Federal Reserve Bank of New York.

The District will have specific written agreements with each firm with which it enters into repurchase agreements.

2. Reverse Repurchase Agreements

The District may enter into reverse repurchase agreements only with primary dealers of the Federal Reserve Bank of New York.

32. Bankers' Acceptances

The District may invest in bankers' acceptances issued by domestic or foreign banks, which are eligible for purchase by the Federal Reserve System, the short-term paper of which is rated in the highest category by a nationally recognized statistical rating organization (NRSRO). (Res. 2011-047, 5/27/11.)

Purchases of bankers' acceptances may not exceed 180 days maturity or 40 percent of the District's surplus money. (Res. 2018-016, 2/23/18.)

43. Negotiable Certificates of Deposit

The senior debt obligations of institutions issuing negotiable certificates of deposit must be rated in one of the three highest categories by a NRSRO. (Res. 2011-047, 5/27/11; Res. 2012-044, 6/22/12; Res. 2015-021, 03/13/15.)

54. Shares of Beneficial Interest

The purchase price of shares of beneficial interest issued by diversified management companies, including those that are money market funds registered with the Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. Sec 80a-1 et seq.), investing in the securities and obligations authorized by the subdivisions of Section 53601, shall not exceed 15 percent of the District's surplus money. (Res. 2009-019, 2/27/09; Res. 2018-016, 2/23/18.)

J. Local Agency Investment Fund

“The District is also authorized to invest in the State of California’s Local Agency Investment Fund (LAI) pursuant to *California Government Code Section 16429.1*, up to the maximum amount allowed by the State Treasurer.” (Res. 2010-037, 5/19/10)

K. Diversification

Except as provided below, no more than five percent (5%) of the District’s surplus funds may be invested in any one institution, inclusive of all sectors. The types of investments which are excluded from this limitation are:

- United States Treasury, federal agency, and United States government-sponsored enterprise obligations;
- Supranational obligations;
- Money market funds and local government investment pools, including LAIF and the California Investment Management Program (CAMP).
(Res. 2018-016, 2/23/18.)

L. Maximum Maturity

Investment maturities shall be based on a review of cash flow forecasts. Maturities will be scheduled so as to permit the District to meet all projected obligations as provided by the Auditor-Controller. (Res. 2018-016, 2/23/18.)

Unless otherwise specified in this section, no investment shall be made in any security, other than a security underlying a repurchase or reverse repurchase agreement as authorized by this section, that at the time of the investment has a term remaining to maturity in excess of five years. (Res. 96-151; Res. 00-155, 7/28/00; Res. 2018-016, 2/23/18.)

M. Ineligible Investments

Any security type or structure not specifically approved by this policy is hereby specifically prohibited. Security types which are thereby prohibited include, but are not limited to,

- ~~"Complex" derivative structures such as range~~Range notes, dual index notes, inverse floaters, leveraged or deleveraged floating-rate notes, ~~or any other complex variable rate or structured note~~and mortgage-derived, interest-only strips.

- ~~Interest only strips that are derived from a pool of mortgages, or a~~Any security that could result in zero interest accrual if held to maturity, ~~except that, in the event of, and for the duration of, a period of negative interest rates, the District may invest in securities issued by, or backed by, the United States government that could result in zero- or negative-interest accrual. This limitation shall not apply to the District's investments in shares of beneficial interest issued by diversified management companies registered under the Investment Company Act of 1940 (15 U.S.C. Sec. 80a-1 et seq.) that are authorized for investment pursuant to subdivision (l) of Section 53601.~~

N. Sales Prior to Maturity

Sales prior to maturity are permitted. Certain investment opportunities may involve the recognition of value losses. Book value trading losses are permitted. Any trading loss greater than 1 percent of principal value of any investment holding requires the following: (1) explanation of source of loss; (2) rationale for transactions resulting in recognition of loss; and, (3) estimation of time necessary to recoup the loss.

O. Reporting Requirements

The Auditor-Controller shall provide to the General Manager, the Finance-Auditing Committee and the Board a monthly investment report, which shall include, at a minimum, the following information for each individual investment:

- Type of investment instrument;
- Issuer name;
- Maturity date;
- Par value;
- Purchase price; and,
- Current market value and the source of the valuation. (Res. 03-035, 4/11/03)

The monthly report also shall: (1) state compliance of the portfolio to the statement of investment policy, or manner in which the portfolio is not in compliance; (2) include a description of any of the District's funds, investments or programs that are under the management of contracted parties, including lending programs; and, (3) include a statement denoting the ability of the District to meet its expenditure requirements for the next six months, or provide an explanation as to why sufficient money shall, or may, not be available.

This monthly report shall be submitted within 30 days following the end of the month.

The Auditor-Controller shall annually render to the Board a statement of investment policy, which the Board shall consider at a public meeting.

P. Safekeeping and Custody

All securities, whether negotiable, bearer, registered, or nonregistered, whether purchased for the District by financial advisors, consultants or managers, shall be delivered, either by book entry or physical delivery, to the District's third party custodian.

Q. Investment Sub-Committee

An Investment Sub-Committee ~~shall be established~~ that will include the Chair of the Finance-Auditing Committee, plus two other Directors and the Auditor-Controller, shall be established to periodically, as needed, to review the District's investment strategy and investment policy. (Res. 81-197, 5/29/81; Res. 2012-044, 6/22/12.)