



October 16, 2020

Memorandum

To: Dustin Claussen, Director of Finance
City of Hayward

From: Monique Spyke, Managing Director
PFM Asset Management LLC

Re: Annual Investment Policy Review

PFM has completed its Investment Policy (the “Policy”) review for the City of Hayward. The Policy is in compliance with the sections of California Government Code (“Code”) that govern the investment of public funds. This year, we are presenting proposed changes to the Policy under two main categories: (1) address recent Code changes that will go into effect on January 1, 2021, and (2) general recommended modifications. These proposed modifications are described in more detail below and in the attached redlined copy of the Policy.

Address Code Changes

On September 28, 2020, Governor Gavin Newsom signed into law Senate Bill 998 (Moorlach) – Local Government Investments (“SB 998”). SB 998, which is set to take 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, including:

- 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);
- 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;
- Establishing a 10% issuer limit on commercial paper and corporate notes for all agencies, other than a county or a city and county; and
- Adding permission for federally recognized Indian tribes to invest and participate in investment JPAs.

We recommend the City edit its Policy to address the first two items listed above.



General Recommended Modifications

IX. Reporting

Code section 53607 states that public agencies shall make a monthly report of transactions to the legislative body. We recommend adding the reference to the Code section to the Policy's Monthly report subsection.

X. Investment Instruments

In order to 1) increase consistency between the investment instrument summary table and the security descriptions listed below the table, 2) better align the Policy with Code, and 3) address SB 998, we are suggesting the following Policy changes.

B. U.S. Agencies. The Policy states that the City may invest up to 100% of the invested funds in securities issued by federal agencies or government-sponsored enterprises (GSEs), and that no more than 40% may be invested in any one federal agency or GSE issuer. Furthermore, the Policy says that no more than 20% may be invested in federal agency mortgage-backed securities (MBS). We are suggesting edits to the Policy's investment summary table so that it clearly reflects these requirements and limitations.

In addition, we have deleted the reference to Code 53601(o) in the Agency paragraph, as that section does not apply to agency MBS, but only to non-agency MBS and asset-backed securities.

C. Commercial Paper. The commercial paper reference in the table and description were modified to address changes made by SB 998.

G. Medium-Term Notes. SB 998 set a 10% limitation on the amount that can be invested in any one commercial paper and medium-term note issuer. While not required prior to SB 998, the City's Policy contains a 5% issuer limit on commercial paper and medium-term notes, as stated in the summary table. We recommend the City maintain its more stringent 5% limit and that the issuer limitation language be added to the medium-term note description, in accordance with SB 998.

J. Other Investment Pools. Effective January 1, 2020, and described below, paragraph (r) was added to Code section 53601. This resulted in a change to language in Code section 53601 (p), other investment pools and we addressed that change in our recommendations.



XI Prohibited Investments

Changes made by SB 998 now allow public agencies to invest in securities issued by, or backed by, the United States 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. While we hope we won't have to buy a security that results in zero or negative interest accrual on behalf of the City, we think it is appropriate to have the option in case it is necessary.

Informational Item

Effective January 1, 2020, Assembly Bill No. 857, provides for the establishment of public banks by local agencies, subject to approval by the Department of Business Oversight (DBO) and Federal Deposit Insurance Corporation (FDIC). As a part of this bill, subsection (r) was added to Code section 53601, which permits local agencies to invest in the commercial paper, debt securities, or other obligations of such public banks.

We are not aware of any such public banks in existence currently and we would want to review the operational history and credit quality of any public bank before we could purchase or recommend the purchase of its securities. As such, we do not recommend that the City add obligations of these public banks to its listing of authorized investment investments at this time. We will continue to monitor any ongoing developments in this area, and if, at a later date, we feel it would be prudent for the City to add this investment type, we will make a formal recommendation at that time.

Please let us know if you have any questions and if you would like to discuss our recommendations further. Thank you.