

Breaking Down the California Government Code & Recent Changes



Presented by:

Sarah Meacham, Program Administrator
meachams@pfm.com

Christopher Presley, Relationship Manager
presleyc@pfm.com
800.729.7665

Review of the California Government Code

Important Codes Related to Government Investments

California Government Code (Code)

- Investment Surplus (53600-53610)
- Deposit of Funds (53630-53686)

The screenshot displays the California Legislative Information website. At the top, there is a navigation bar with links for Home, Bill Information, California Law, Publications, Other Resources, My Subscriptions, and My Favorites. A search bar is located in the top right corner. Below the navigation bar, the page title is "California Law >>> Code Section Group". The main content area shows the following structure:

- GOVERNMENT CODE - GOV
 - TITLE 5. LOCAL AGENCIES [50001 - 57550] (Title 5 added by Stats. 1949, Ch. 81.)
 - DIVISION 2. CITIES, COUNTIES, AND OTHER AGENCIES [53000 - 56821] (Division 2 added by Stats. 1949, Ch. 81.)
 - PART 1. POWERS AND DUTIES COMMON TO CITIES, COUNTIES, AND OTHER AGENCIES [53000 - 54999.7] (Part 1 added by Stats. 1949, Ch. 81.)
 - CHAPTER 4. Financial Affairs [53600 - 53997] (Chapter 4 added by Stats. 1949, Ch. 81.)
 - ARTICLE 1. Investment of Surplus [53600 - 53610] (Article 1 added by Stats. 1949, Ch. 81.)

The text of Article 1, Section 53600 is displayed below the structure:

53600. As used in this article, "local agency" means county, city, city and county, including a chartered city or county, school district, community college district, public district, county board of education, county superintendent of schools, or any public or municipal corporation.
(Amended by Stats. 1987, Ch. 887, Sec. 2.)

53600.3. Except as provided in subdivision (a) of Section 27000.3, all governing bodies of local agencies or persons authorized to make investment decisions on behalf of those local agencies investing public funds pursuant to this chapter are trustees and therefore fiduciaries subject to the prudent investor standard. When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency. Within the limitations of this section and considering individual investments as part of an overall strategy, investments may be acquired as authorized by law.

Who Do the Codes Apply to?

53600 defines a “local agency” as any:

- County
- City
- City and County
- Public District
- Public or Municipal Corporation
- School District
- Community College District
- County Board of Education
- County Superintendent of Schools

} Typically required to invest through County Treasury

Standard of Prudence (53600.3)

- Code defines the standard of prudence for public funds to be the Prudent Investor Standard, which states that:

“When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency.”

- Members of council/board and anyone authorized to make investment decisions are considered trustees and fiduciaries subject to this standard of prudence
- Permits investments to be acquired
- Consider investments as part of overall strategy/portfolio

Objectives (53600.5)

1

Safeguard
Principal



2

Meet Liquidity
Needs



3

Achieve
a Return



Application of 53601

Agency types:

- Cities, districts, and local agencies who do not pool money in deposits or investments with other local agencies with different governing bodies

Fund types:

- Sinking funds or moneys in treasury not immediately required

Delivery of securities:

- Must be in agency's name and delivered to the agency or a third-party custodian

Application of percentage limits:

- Date of purchase

Maximum maturity:

- Five years unless otherwise stated or council/board has approved longer-term investments at least 90-days in advance

Applying the Code

Investment Universe vs. California Government Code

Securities	1 Day	180 Days	270 Days	1 Year	5 Years	Over 5 Years
U.S. Treasuries		✓ Permitted				Requires Approval
Federal Agencies		✓ Permitted				Requires Approval
Municipal Securities		✓ Permitted				Requires Approval
Negotiable Certificates of Deposit		✓ Permitted				Requires Approval
Commercial Paper	✓ Permitted				X Prohibited	
Bankers' Acceptances	✓ Permitted				X Prohibited	
Medium-Term Corporate Notes		✓ Permitted				X Prohibited
Asset-Backed Securities (ABS)		✓ Permitted				X Prohibited
Supranationals		✓ Permitted				X Prohibited
Repurchase Agreements		✓ Permitted			X Prohibited	
Money Market Funds/Bond Mutual Funds	✓ Permitted				X Prohibited	
Local Government Investment Pools	✓ Permitted				X Prohibited	
Foreign Sovereign						X Prohibited
Fixed-Income ETFs						X Prohibited
High-Yield Bonds						X Prohibited
Private Placements						X Prohibited
Convertibles						X Prohibited
Non-U.S. Dollar Investment Grade						X Prohibited
Emerging Markets Debt						X Prohibited
Bank Loans						X Prohibited
Domestic Equities (Large, Mid, Small Cap)						X Prohibited
International Equities (Large, Mid, Small Cap)						X Prohibited
Emerging Markets						X Prohibited
Preferred Stock						X Prohibited
Equity Mutual Funds and ETFs						X Prohibited
Commodities						X Prohibited
Real Estate						X Prohibited
Hedge Funds						X Prohibited
Private Equity						X Prohibited
Venture Capital						X Prohibited
Tangible Assets						X Prohibited
Complex Derivatives, Futures and Options						X Prohibited

Permitted Investments – Government Sector

U.S. Treasuries (b)

Federal Agencies (f)

Local agency's own bonds (a)

State of California bonds (c)

California local agency bonds (e)

Bonds issued by 49 other states (d)

Supranationals (q)

- Issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank
- 30% of portfolio
- 5-year maximum maturity
- AA or better by an NRSRO

Permitted Investments – Non-Government Sector

Bankers' acceptances (g)

- 40% of portfolio
- 180 day maximum maturity

Commercial paper (h)

- 25% of portfolio
- 270 day maximum maturity
- 10% of the outstanding CP of any single issuer
- Credit criteria

Negotiable CDs (i)

- Issued by nationally or state-chartered bank, savings association, federal association, state or federal credit union, or by a federally- or state-licensed bank branch of a foreign bank
- 30% of portfolio
- Conflict of interest limitation

Permitted Investments – Non-Government Sector

Repurchase and reverse repurchase agreements (j)

- 1 year/92 day maximum maturity
- Counterparty, collateral, and other requirements

Medium-term notes (k)

- 30% of portfolio
- 5-year maximum maturity
- Issued by corporations organized and operating in U.S. or depository institutions licensed by U.S. or any state and operating in U.S.
- A or better

Mortgage- or asset-backed securities (o)

- 20% of portfolio
- 5-year maximum maturity
- AA or better by an NRSRO

Permitted Investments – Pooled

Shares of beneficial interest issued by a diversified management company (I)

- Money market mutual funds (2)
 - 20% of portfolio
 - AAA by two or more NRSROs OR Advisor requirements
 - Net asset value (NAV) may be stable or variable depending on type of fund (government vs. prime, retail vs. institutional)
- Mutual funds (1)
 - 20% of portfolio, no more than 10% in any one fund
 - AAA by two or more NRSROs OR Advisor requirements
 - Variable net asset value (NAV)
 - Underlying investments must be same as California Government Code Section 53601

Key Elements of Money Market Reform

After the 2008-2009 financial crisis, the Securities and Exchange Commission (SEC) tightened certain risk-limiting provisions of the regulations that govern money market funds by adopting significant changes to Rule 2a7.

	Prime Fund	Government Fund
	Government securities, commercial paper, certificates of deposit, corporate notes and other debt investments	99.5% of total assets in cash, government securities or repos
Retail Fund Limited to “natural persons”	<ul style="list-style-type: none"> • Constant NAV • Gates • Liquidity Fees 	<ul style="list-style-type: none"> • Constant NAV • Optional Gates • Optional Liquidity Fees
Institutional Fund	<ul style="list-style-type: none"> • Variable NAV • Gates • Liquidity Fees 	<ul style="list-style-type: none"> • Constant NAV • Optional Gates • Optional Liquidity Fees

Permitted Investments – Pooled (cont'd)

- Shares of beneficial interest issued by a joint powers authority (p)
 - Local government investment pools (LGIPs), including CAMP
 - Adviser requirements
- State of California's Local Agency Investment Fund (LAIF) (16429.1)
- County Treasurers' pools (53684)



Permitted Investments (53635)

- For agencies that pool money with other local agencies that have different governing bodies
- Difference from 53601
 - 40% of portfolio in commercial paper
 - 10% of portfolio in commercial paper of any one issuer

History of Changes 2001-2002

January 1, 2001

- SB 68 designated money in the Local Agency Investment Fund (LAIF) as non-state money

January 1, 2002

- AB 609:
 - Clarified which agencies fall under 53601 (all local agencies that are not counties) and 53635 (applies only to counties and certain pools)
 - Simplified definition of Federal Agencies by eliminating references to specific Agencies
 - Changed sliding scale of permitted commercial paper allocation to static 25%
 - Added Fitch to the list of rating agencies providing ratings for commercial paper
 - Eliminated distinction between pre- and post-December 1994 investments for repurchase and reverse repurchase agreements and securities lending
 - Added Community Redevelopment Act rating of satisfactory for depositories to be eligible to receive funds
 - LAIF's deposit limit goes from \$30 million to \$40 million

History of Changes 2004-2012

January 1, 2004	<ul style="list-style-type: none">• SB 787 replacing references to specific rating agencies with “nationally recognized statistical-rating organization (NRSRO)”
September 30, 2004	<ul style="list-style-type: none">• AB 2853 made the submission of investment policies and quarterly reports optional and therefore not a reimbursable mandate
January 1, 2005	<ul style="list-style-type: none">• AB 969 added 2 new sections, 6509.7 and 53601(p), that provide specific criteria and authorization for the formation and use of joint powers authorities for pooling funds for investment purposes
January 1, 2007	<ul style="list-style-type: none">• AB 2011 added 2 new Code sections, 53601.8 and 53635.8, explicitly allowing use of CD placement services through January 1, 2012
January 1, 2008	<ul style="list-style-type: none">• AB 1745 added a new section, 53601(d), that allows municipal bonds from any of the other 49 states
November 16, 2009	<ul style="list-style-type: none">• LAIF’s deposit limit goes from \$40 million to \$50 million
January 1, 2011	<ul style="list-style-type: none">• SB 1344 removed January 1, 2012 sunset date for eligibility of CD placement services
January 1, 2012	<ul style="list-style-type: none">• SB 194 added federally-licensed branch of a foreign bank to list of eligible issuers for negotiable CDs

Recent Changes to Code

January 1, 2014

- AB 279 added two sections each for 53601.8 and 53635.8:
 - Section 1 of 53601.8 and Section 3 of 53635.8, which took effect January 1, 2014 and set to expire December 31, 2016, expanded the types of deposits that local agencies can invest in using a deposit placement service. Added a 10% limit for any one placement service.
 - Section 2 of 53601.8 and Section 4 of 53635.8, which was scheduled to take effect January 1, 2017, would revert the Code back to prior language, again limiting deposits to CDs. No expiration date was defined.

January 1, 2015

- AB 1933 added section 53601(q) that permits local agencies to invest in the senior debt obligations of three specific U.S. Instrumentalities: the International Bank for Reconstruction and Development, International Finance Corporation, and the Inter-American Development Bank.
- AB 283 extended the dates established in AB 279.

January 1, 2016

- Section 1 of 53601.8 and Section 3 of 53635.8 sunset dates were extended from January 1, 2017 to January 1, 2021. Eliminated the combined 30% holding limits for placement service CDs and negotiable CDs. Eliminated the 10% limits for any one placement service.
- Section 2 of 53601.8 and Section 4 of 53635.8 are scheduled to take effect January 1, 2021 and will last indefinitely.

Recent Changes to Code (cont'd)

January 1, 2017

- SB-974 clarified the Code's rating requirements such that a required rating is for the entire category and not for a specific rating.

January 1, 2019

- AB 1770 revised language in section 53601(o) to permit the purchase of ABS with a maximum remaining maturity of 5 years and eliminate the requirement that issuers be rated "A" or better by an NRSRO.

Authorized Securities Dealers (53601.5)

- Direct issuers
- Broker-dealer registered with California
- Member of a federally regulated securities exchange (i.e., FINRA)
- National or state-chartered bank
- Savings or federal association
- Primary dealers

The screenshot displays the Federal Reserve Bank of New York website. The header includes navigation links: MUSEUM & GOLD TOUR, DATA & STATISTICS, CAREERS, BLOG, and PRESS CENT. The main navigation bar lists: About the New York Fed, Markets & Policy Implementation, Economic Research, and Financial Institution Supervision. The breadcrumb trail reads: home > markets & policy implementation > counterparties >. The page title is "Primary Dealers". The text states: "Primary dealers are trading counterparties of the New York Fed in its implementation of monetary policy. They are also expected to make markets for the New York Fed on behalf of its official accountholders as needed, and to bid on a pro-rata basis in all Treasury auctions at reasonably competitive prices." Below this is a section titled "LIST OF PRIMARY DEALERS" with a sub-section "CURRENT LIST, ADDITIONS, REMOVALS & NAME CHANGES". A tabbed interface shows "PRIMARY DEALERS" selected. The list of primary dealers is as follows:

Bank of Nova Scotia, New York Agency	J.P. Morgan Securities LLC
BMO Capital Markets Corp.	Merrill Lynch, Pierce, Fenner & Smith Incorporated
BNP Paribas Securities Corp.	Mizuho Securities USA LLC
Barclays Capital Inc.	Morgan Stanley & Co. LLC
Cantor Fitzgerald & Co.	NatWest Markets Securities Inc.
Citigroup Global Markets Inc.	Nomura Securities International, Inc.
Credit Suisse AG, New York Branch	RBC Capital Markets, LLC
Daiwa Capital Markets America Inc.	Societe Generale, New York Branch
Deutsche Bank Securities Inc.	TD Securities (USA) LLC
Goldman Sachs & Co. LLC	UBS Securities LLC.
HSBC Securities (USA) Inc.	Wells Fargo Securities, LLC

Source: <https://www.newyorkfed.org/markets/primarydealers#primary-dealers>.

Prohibited Investments (53601.6)

- Inverse floaters
- Range notes
- Mortgage-derived, interest-only strips
- Security that could result in zero interest accrual if held to maturity
- Exempts mutual funds



Deposit Placement Services (53601.8)

- 30% of portfolio
- Depository institution must have branch in California and be one of these types of financial institutions:
 - Nationally or state-chartered commercial bank
 - Savings bank
 - Savings and loan association
 - Credit union
- Must be FDIC or NCUA insured



Other Permissions

1

Can purchase investments through primary or secondary markets (53603)

2

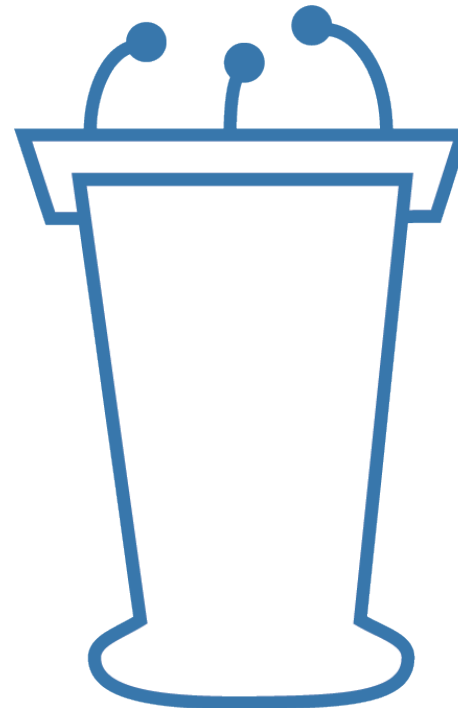
May sell or exchange investments prior to maturity (53604)

3

May sell to raise cash for agency's expenditures (53605)

Delegation of Authority (53607)

- Council/board may delegate to Treasurer for one-year period
- Must be renewed annually
- Must make monthly report of transactions when authority is delegated
 - **Commonly missed reporting requirement**



Reporting Requirements (53646)

- Quarterly reporting requirements are optional
- If providing quarterly reports, they must:
 - Be submitted within 30 days after quarter end
 - Include: investment type, issuer, maturity date, par amount, purchase price, description of funds being managed by an outside party, market value and source for any securities managed by an outside party that is not a local agency or LAIF
 - State that the portfolio is in compliance with the Policy or manner in which it is out of compliance
 - State the ability of the agency to meet its pool's expenditure requirements for the next 6 months or explain why it cannot

Reporting Requirements (53646)



Managed Account Detail of Securities Held

For the Month Ending December 31, 2018

Security Type/Description Dated Date/Coupon/Maturity	CUSIP	S&P Par	Moody's Rating	Trade Date	Settle Date	Original Cost	YTM at Cost	Accrued Interest	Amortized Cost	Market Value	
Supra-National Agency Bond / Note											
INTER-AMERICAN DEVELOPMENT BANK DTD 11/08/2013 2.125% 11/09/2020	4581X0CD8	415,000.00	AAA	Aaa	10/02/17	10/10/17	418,846.68	1.81	1,273.82	417,343.67	411,126.81
INTERNATIONAL FINANCE CORPORATION NOTE DTD 03/16/2018 2.635% 03/09/2021	45950VLO7	1,000,000.00	AAA	Aaa	03/09/18	03/16/18	999,250.00	2.66	8,197.78	999,441.28	998,867.00
INTL BANK OF RECONSTRUCTION AND DEV NOTE DTD 07/25/2018 2.750% 07/23/2021	459058GH0	1,570,000.00	AAA	Aaa	07/18/18	07/25/18	1,566,326.20	2.83	18,709.17	1,566,838.11	1,576,385.19
INTER-AMERICAN DEVEL BANK DTD 09/14/2017 1.750% 09/14/2022	4581X0CZ9	1,080,000.00	AAA	Aaa	02/21/18	02/23/18	1,032,760.80	2.78	5,617.50	1,041,194.08	1,045,584.72
Security Type Sub-Total		5,860,000.00					5,808,806.43	2.36	42,517.91	5,817,874.46	5,795,084.49
Municipal Bond / Note											
CA ST TXBL GO BONDS DTD 04/25/2018 2.800% 04/01/2021	13063DGA0	635,000.00	AA-	Aa3	04/18/18	04/25/18	635,025.40	2.80	4,445.00	635,014.19	634,441.20
Security Type Sub-Total		635,000.00					635,025.40	2.80	4,445.00	635,014.19	634,441.20
Federal Agency Collateralized Mortgage Obligation											
FNMA SERIES 2015-M15 ASQ2 DTD 11/01/2015 1.898% 01/01/2019	3136A0SW1	7,367.51	AA+	Aaa	11/06/15	11/30/15	7,441.18	1.20	11.65	7,367.51	7,352.12
FHLMC SERIES KP03 A2 DTD 04/01/2016 1.780% 07/01/2019	3137BNN26	164,684.29	AA+	Aaa	04/15/16	04/28/16	166,327.18	1.10	244.28	164,755.18	163,668.27
FANNIE MAE SERIES 2015-M13 ASQ2 DTD 10/01/2015 1.646% 09/01/2019	3136A0DQ0	42,849.69	AA+	Aaa	10/07/15	10/30/15	43,278.78	1.08	58.78	42,877.55	42,590.07
FVA 2018-M5 A2 DTD 04/01/2018 3.560% 09/25/2021	3136B1XP4	629,062.54	AA+	Aaa	04/11/18	04/30/18	641,575.23	2.27	1,866.22	639,200.80	636,128.11
FHLMC MULTIFAMILY STRUCTURED P POOL DTD 12/01/2015 3.090% 08/25/2022	3137BM6P6	840,000.00	AA+	Aaa	04/04/18	04/09/18	847,153.13	2.61	2,163.00	845,781.44	844,112.05

Investment Type

Maturity Date

Issuer

Par Amount

Purchase Price

Market Value

Investment Policies (53646)

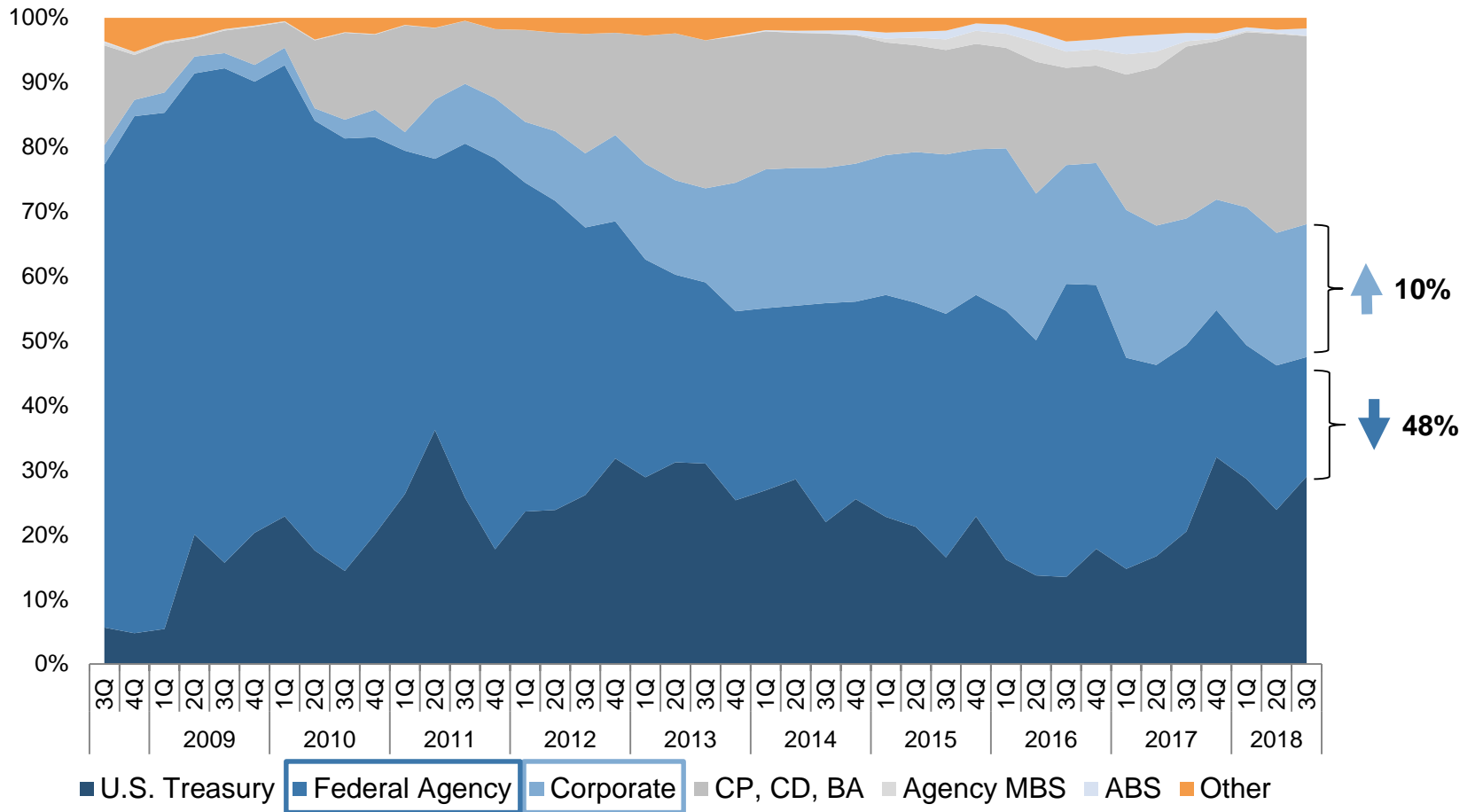
Local agencies

- May annually render a statement of investment policy to council/board/oversight committee, which shall be considered at a public meeting by the council/board
- Any change in the Policy shall be **considered** by the council/board at a public meeting

Counties

- May annually render to the board of supervisors/oversight committee a statement of investment policy, which board shall review and approve at a public meeting
- Any change in the Policy shall be **reviewed and approved** by the board at a public meeting

Public Agencies' Portfolios Have Changed



Source: PFM 1-3 Year Fixed Income Composite.

Common Misconceptions When Applying California Code

Misconception: Utilizing permitted non-government sectors adds too much risk.

Truth: California Government Code is inherently risk averse.

Misconception: The more specific you are in your investment policy, the better you're managing risk.

Truth: Flexibility within the parameters of California Government Code is sufficient risk management. The Code is designed to protect portfolios while providing flexibility to make strategic movements.

Misconception: Legacy investment parameters as established in my agency's investment policy don't need to change.

Truth: What worked then, might not work now.

Disclaimer

*This information is for institutional investor use only, not for further distribution to retail investors, and does not represent an offer to sell or a solicitation of an offer to buy or sell any fund or other security. Investors should consider the Trust's investment objectives, risks, charges and expenses before investing in the Trust. This and other information about the Trust is available in the Trust's current Program Guide, which should be read carefully before investing. A copy of the Trust's Program Guide may be obtained by calling 1-800-729-7665 or is available on the Trust's website at www.camponline.com. While the Trust seeks to maintain a stable net asset value of \$1.00 per share, it is possible to lose money investing in the Trust. An investment in the Trust is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Shares of the Trust are distributed by **PFM Fund Distributors, Inc.**, member Financial Industry Regulatory Authority (FINRA) (www.finra.org) and Securities Investor Protection Corporation (SIPC) (www.sipc.org). PFM Fund Distributors, Inc. is a wholly owned subsidiary of PFM Asset Management LLC.*

PFM Asset Management LLC ("PFM") serves as CAMP's Program Administrator, Investment Adviser and Rebate Calculation Agent. PFM specializes in meeting the investment needs of public agencies. PFM is registered as an investment adviser with the Securities and Exchange Commission ("SEC") under the Investment Advisers Act of 1940.

Appendix

Resources

California

California Government Code



California Municipal Treasurers Association



California Debt and Investment Advisory
Commission Local Agency Investment
Guidelines



National

Association of Public Treasurers



Government Finance Officers Association



CFA Institute

