

# **OPEN SESSION AGENDA ITEM**

**54-143 MAY 2018  
F&P COMMITTEE ITEM III.C.**

**DATE:** May 17, 2018  
**TO:** Members, Finance and Planning Committee  
**FROM:** Kevin Harper, Interim Chief Financial Officer  
**SUBJECT:** Investment Policy Revision

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## **EXECUTIVE SUMMARY**

The State Bar's Investment Policy (Tab 4.4, Article 1, Sections 1 - 8 of the Board Book) requires that the investment policy be reviewed annually. This agenda item represents that annual review of the policy. Certain updates and improvements to the Investment Policy are proposed.

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## **BACKGROUND**

The State Bar's Investment Policy (per Tab 4.4, Article 1, Sections 1 - 8 of the Board Book) outlines the State Bar's investment objectives, identifies authorized investment instruments, and identifies responsibilities. The policy is designed as a broad framework for the Bar's investments and is not intended to provide specific procedures for the purchase of individual investments. Key elements of the Investment Policy are:

- Section 1 – Policy Statement specifies the State Bar's policy as follows: "It is the policy of the State Bar of California to invest public funds in a manner which will provide the maximum security with best investment return, while meeting the daily cash flow demands of the Bar and conforming to all State statutes governing the investment of public funds and all Resolutions of the Board of Trustees."
- Section 2 – Objectives, discusses various investment objectives including diversification, identifies funds subject to the policy, requires safety of principal as the foremost objective and requires an independent third-party custodian.
- Section 3 – Investment Instruments Authorized by the State of California, identifies the investments that the Bar is allowed to purchase and hold.
- Section 4 – Reports of Investment Activities, calls for quarterly reports to the Board of Trustees on the status of the Bar's investment portfolio.
- Section 5 – Ethics and Conflicts of Interest, discusses avoidance of conflicts.
- Section 6 – Required Review of State Bar Investment Policy, requires annual review of the policy.

## **DISCUSSION**

Staff recommends that the Investment Policy be revised to incorporate the updates and improvements shown below. Certain revisions to the Investment Policy adopted by the Board Planning and Budget Committee on November 17, 2016 were not reflected in the Board Book and are repeated herein.

- A sentence is added to Section 2b clarifying that the amount of each type of investment shall be limited by portfolio limits imposed on local governments by the State of California as shown in Section 3.
- The table in Section 3 showing allowable investments is updated to the most recent list allowed by the State of California for local governments.
- References to the Investment Advisory Subcommittee are removed since it no longer exists.
- A “Responsible Official” paragraph is added to Section 2 to specify the Chief Financial Officer as the official responsible for buying and selling investments.
- The section that defines “Surplus Funds” is removed because that term is not used in the policy.

The proposed revisions to the Investment Policy are shown in Attachment A (redline version) and Attachment B (clean version).

## **FISCAL/PERSONNEL IMPACT**

None

## **RULE AMENDMENTS**

None

## **BOARD BOOK AMENDMENTS**

Main Section 4, Tab 4.4, Article 1, Section 1 to 8, Page 1-6

## **STRATEGIC PLAN GOALS & OBJECTIVES**

Goal: 3. Improve the fiscal and operational management of the State Bar, emphasizing integrity, transparency, accountability, and excellence.

Objective: d. Reallocate funds to support the discipline system based on expenditure review, revenue enhancement measures, implementation of the Bar’s reserve policy, and other reengineering efforts.

## **RECOMMENDATION**

It is recommended that the **Finance and Planning Committee** approve the following resolution:

**RESOLVED**, that the Finance and Planning Committee directs staff to amend Board Book Tab 4.4, Article 1, Sections 1 to 8, to reflect the proposed changes.

## **ATTACHMENT(S) LIST**

- A.** Investment Policy, with proposed changes – redline version
- B.** Investment Policy, with proposed changes – clean version

**TAB 4.4**

**INVESTMENT POLICY**

**Article 1 INVESTMENT POLICY**

Section 1 Policy Statement

Section 2 Objectives

Section 3 Investment Instruments Authorized by the State of California

Section 4 ~~Surplus Funds~~ Reports of Investment Activities

Section 5 ~~Reports of Investment Activities~~ Ethics and Conflicts of Interest

Section 6 ~~Ethics and Conflicts of Interest~~ Required Review of State Bar Investment Policy

~~Section 7~~ Required Review of State Bar Investment Policy

~~Section 8~~ Investment Advisory Subcommittee

## **Article 1 INVESTMENT POLICY**

### **Section 1    Policy Statement**

It is the policy of the State Bar of California to invest public funds in a manner which will provide the maximum security with best investment return, while meeting the daily cash flow demands of the Bar and conforming to all State statutes governing the investment of public funds and all Resolutions of the Board of Trustees.

### **Section 2    Objectives**

(a)    Safety Of Invested Funds

- (1) Minimum Standards: —Investment instruments must conform to the standards established by the State of California as set forth in Section 3. As these standards are modified by the State from time to time, this investment policy will automatically adopt the revised standards.
- (2) Diversification: To minimize risk of loss, the State Bar shall diversify its investment portfolio utilizing any combination of investment instruments specified in Section 3. The maximum amount the State Bar invests in each type of investment instrument is limited to the “maximum specified % of portfolio” shown in Section 3.
- (3) Scope: This investment policy applies to all financial assets under direct control of the State Bar, including all of the funds accounted for in the State Bar quarterly report to the Board and include the General Fund, Restricted Funds, and other funds that may be created from time to time. The State Bar holds no pension trust funds for which it is accountable.

This policy does not apply to investment activities of moneys held by a trustee or fiscal agent and pledged to the payment or security of bonds or other indebtedness, or obligations under a lease, installment sale, or certificates of participation. Such funds are invested in accordance with the statutory provisions governing the issuance, or in the absence of specific statutory provisions, in accordance with the ordinance, resolution, indenture, or agreement of the State Bar of California providing for the issuance. These funds are identified as the State Bar of California Section 457 Deferred Compensation Plan and the Post Employment Benefit Fund.

- (4) Safety of Principal: Safety of principal is the foremost objective of the investment policy. Investments of the State Bar of California shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio.

(5) Custodianship of Instruments: The State Bar will utilize an independent third party custodian to provide custodial services on all of the State Bar's investments.

(6) 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. This standard of prudence shall be applied in the context of managing an overall portfolio. Investment officials acting in accordance with the investment policy and exercising due diligence shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided that deviations from expectation are reported in a timely fashion, and appropriate action is taken to mitigate adverse developments<sup>1</sup>.

(b) Liquidity Of Invested Funds: The State Bar's investment portfolio will remain sufficiently liquid to enable the State Bar to meet all operating requirements that might be reasonably anticipated.

(c) Return on Investment: The State Bar's investment policy shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, commensurate with the State Bar's investment risk constraints and the cash flow characteristics of the portfolio. Investments shall be made with the intent to hold to maturity unless the liquidity needs of the portfolio require that the security be sold or a capital gain be realized in a manner that better positions the overall portfolio in achieving investment policy goals. ~~The Finance Director is designated as the official with responsibility for authorizing the sale or liquidation of investments in advance of their scheduled maturity dates.~~

(d) Responsible Official: The Chief Financial Officer is designated as the official with responsibility for authorizing the following:

- Opening and closing accounts
- Selection of investment managers and custodians
- Purchase of investments
- Sale or liquidation of investments prior to their scheduled maturity dates.

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<sup>1</sup> Pursuant to Government Code sections 825 and 995, the State Bar is required to indemnify the Board of Trustees, its officers and other employees.

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(2)(e) Authorized Financial Dealers and Financial Institutions: The ~~Finance Director~~Chief Financial Officer of the State Bar will maintain a list of financial institutions authorized to provide investment services. In addition, a list will also be maintained of approved security broker/dealers, selected by credit worthiness, who are authorized to provide investment services in the State of California.

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(f) Distribute Investment Policy: The State Bar shall send a copy of the current investment policy to all parties approved to do business with the State Bar. Confirmation of receipt of this policy shall be considered evidence that the dealer understands the State Bar's investment policies, and intends to show the State Bar of California only appropriate investments.

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(g) Service Provider Controls: The State Bar shall annually obtain and review the System and Organization Controls (SOC1) reports of custodians and investment managers each year to ensure reliability of data and reports received.

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### Section 3 Investment Instruments Authorized By The State Of California

The following table identifies the investment instruments, maturities, portfolio percentage restrictions and other minimum quality requirements established under California Law.

<b>The State Bar of California</b> <b>Investment Policy</b> <b>Investment Instruments Authorized by the State of California</b>			
<b>INVESTMENT TYPE</b>	<b>MAXIMUM MATURITY</b>	<b>MAXIMUM SPECIFIED % OF PORTFOLIO</b>	<b>MINIMUM QUALITY REQUIREMENTS</b>
<u>Local Agency Bonds</u>	<u>5 years</u>	<u>None</u>	<u>None</u>
<u>U.S. Treasury Obligations</u>	<u>5 years</u>	<u>None</u>	<u>None</u>
<u>State Obligations— CA And Others</u>	<u>5 years</u>	<u>None</u>	<u>None</u>
<u>CA Local Agency Obligations</u>	<u>5 years</u>	<u>None</u>	<u>None</u>
<u>U.S Agency Obligations</u>	<u>5 years</u>	<u>None</u>	<u>None</u>
<u>Bankers' Acceptances</u>	<u>180 days</u>	<u>40%</u>	<u>None</u>
<u>Commercial Paper— Pooled Funds</u>	<u>270 days</u>	<u>40% of the agency's money</u>	<u>Highest letter and number rating by an NRSRO</u>
<u>Commercial Paper— Non-Pooled Funds</u>	<u>270 days</u>	<u>25% of the agency's money</u>	<u>Highest letter and number rating by an NRSRO</u>
<u>Negotiable Certificates of Deposit</u>	<u>5 years</u>	<u>30%</u>	<u>None</u>
<u>Non-negotiable Certificates of Deposit</u>	<u>5 years</u>	<u>None</u>	<u>None</u>
<u>Placement Service Deposits</u>	<u>5 years</u>	<u>30%</u>	<u>None</u>
<u>Placement Service Certificates of Deposit</u>	<u>5 years</u>	<u>30%</u>	<u>None</u>
<u>Repurchase Agreements</u>	<u>1 year</u>	<u>None</u>	<u>None</u>
<u>Reverse Repurchase Agreements and Securities Lending Agreements</u>	<u>92 days</u>	<u>20% of the base value of the portfolio</u>	<u>None</u>
<u>Medium-Term Notes</u>	<u>5 years</u>	<u>30%</u>	<u>"A" rating category or its equivalent or better</u>
<u>Mutual Funds And Money Market Mutual Funds</u>	<u>N/A</u>	<u>20%</u>	<u>Multiple</u>
<u>Collateralized Bank Deposits</u>	<u>5 years</u>	<u>None</u>	<u>None</u>
<u>Mortgage Pass-Through Securities</u>	<u>5 years</u>	<u>20%</u>	<u>"AA" rating category or its equivalent or better</u>
<u>County Pooled Investment Funds</u>	<u>N/A</u>	<u>None</u>	<u>None</u>
<u>Joint Powers Authority Pool</u>	<u>N/A</u>	<u>None</u>	<u>Multiple</u>
<u>Local Agency Investment Fund (LAIF)</u>	<u>N/A</u>	<u>None</u>	<u>None</u>

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<u>Voluntary Investment Program Fund</u>	<u>N/A</u>	<u>None</u>	<u>None</u>
<u>Supranational Obligations</u>	<u>5 years</u>	<u>30%</u>	<u>"AA" rating category or its equivalent or better</u>

Investment Type	Maximum Maturity	Maximum Specified % of Portfolio	Minimum Quality Requirements
Local Agency Bonds	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
State of California Obligations	5 years	None	None
CA Local Agency Obligations	5 years	None	None
U.S. Agencies	5 years	None	None
Bankers' Acceptances	180 days	40 percent	None
Commercial Paper—Select Agencies	270 days	25 percent of the agency's money	"A-1/P-1/F-1"; if the issuer has issued long-term debt it must be rated "A" without regard to modifiers
Commercial Paper—Other Agencies	270 Days	40 percent of the agency's money	"A-1/P-1/F-1"; if the issuer has issued long-term debt it must be rated "A" without regard to modifiers
Negotiable Certificates of Deposit	5 years	30 percent	None
Repurchase Agreements	1 year	None	None
Reverse Repurchase Agreements	92 days	20 percent of the base value of the portfolio	None
Medium-Term notes	5 years	30 percent	"A" rating
Mutual Funds	N/A	20 percent	See Footnote <sup>2</sup>
Money Market Mutual Funds	N/A	20 percent	See Footnote <sup>3</sup>
Collateralized Bank Deposits	5 years	None	None
Mortgage Pass-Through Securities	5 years	20 percent	"AA" Rating
Time Deposits	5 years	20 percent	None
County Pooled Investment Funds	N/A	None	None
Local Agency Investment Fund	N/A	None	None

#### ***Section 4 — Surplus Funds***

Surplus funds are defined as those funds not immediately needed for State Bar operations. Surplus funds, however, do not include those minimum balances required by the State Bar's bank to compensate it for the cost of bank services.

#### **Section 45 Reports Of Investment Activities**

The ~~Finance Director~~Chief Financial Officer will make quarterly reports to the Board of Trustees on the status of the State Bar's Investment portfolio. These reports shall include information as to the type of investment, the amount of money invested with various institutions, market value for securities with a maturity of more than 12 months, purchase and maturity dates, rate of interest, and statement of portfolio liquidity, as required by California state law.

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#### **Section 56 Ethics And Conflicts Of Interest**

Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions. Investment officials and employees shall disclose any financial interests as required by the Conflict of Interest Code for Designated Employees of The State Bar of California and the Conflict of Interest Code for the State Bar Board of Trustees. All persons authorized to place or approve investments shall report annually on Form 700 of the California Fair Political Practices Commission all required economic interests for that year.

#### **Section 67 Required Review Of State Bar Investment Policy**

This investment policy shall be reviewed at least annually for the purpose of recommending needed changes and modifications. The Chair of the ~~Investment Advisory Subcommittee~~Finance and Planning Committee will be responsible for initiating the review.

## **~~Section 8—Investment Advisory Subcommittee~~**

~~The Board Planning, Program Development and Budget Committee, will appoint the Chair to the Investment Advisory Subcommittee. The Investment Advisory Subcommittee will consist of four members: the Chair shall be a member of the Board Planning, Program Development and Budget Committee, and the remaining three members may be members of the Board of Trustees and/or individuals with expertise in investment management. The Board Committee shall review the qualifications of, and appoint these non-Board members to serve a one-year term. The Office of Finance shall provide staff support for the committee.~~

~~Meetings of the Committee shall be scheduled on a quarterly basis.~~

(Source: Board of Governors' Resolutions, September 1996, June 2000, September 2000, May 2005; Planning and Budget Committee Resolution, November 19, 2015; Finance and Planning Committee Resolution, November 17, 2016.)

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**TAB 4.4**

**INVESTMENT POLICY**

**Article 1 INVESTMENT POLICY**

*Section 1 Policy Statement*

*Section 2 Objectives*

*Section 3 Investment Instruments Authorized by the State of California*

*Section 4 Reports of Investment Activities*

*Section 5 Ethics and Conflicts of Interest*

*Section 6 Required Review of State Bar Investment Policy*

## **Article 1 INVESTMENT POLICY**

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- (3) Scope: This investment policy applies to all financial assets under direct control of the State Bar, including all of the funds accounted for in the State Bar quarterly report to the Board and include the General Fund, Restricted Funds, and other funds that may be created from time to time. The State Bar holds no pension trust funds for which it is accountable.

This policy does not apply to investment activities of moneys held by a trustee or fiscal agent and pledged to the payment or security of bonds or other indebtedness, or obligations under a lease, installment sale, or certificates of participation. Such funds are invested in accordance with the statutory provisions governing the issuance, or in the absence of specific statutory provisions, in accordance with the ordinance, resolution, indenture, or agreement of the State Bar of California providing for the issuance. These funds are identified as the State Bar of California Section 457 Deferred Compensation Plan and the Post Employment Benefit Fund.

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- (b) Liquidity Of Invested Funds: The State Bar's investment portfolio will remain sufficiently liquid to enable the State Bar to meet all operating requirements that might be reasonably anticipated.
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- (d) Responsible Official: The Chief Financial Officer is designated as the official with responsibility for authorizing the following:
- Opening and closing accounts
  - Selection of investment managers and custodians
  - Purchase of investments
  - Sale or liquidation of investments prior to their scheduled maturity dates.

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<sup>1</sup> Pursuant to Government Code sections 825 and 995, the State Bar is required to indemnify the Board of Trustees, its officers and other employees.

- (e) **Authorized Financial Dealers and Financial Institutions:** The Chief Financial Officer of the State Bar will maintain a list of financial institutions authorized to provide investment services. In addition, a list will also be maintained of approved security broker/dealers, selected by credit worthiness, who are authorized to provide investment services in the State of California.
- (f) **Distribute Investment Policy:** The State Bar shall send a copy of the current investment policy to all parties approved to do business with the State Bar. Confirmation of receipt of this policy shall be considered evidence that the dealer understands the State Bar's investment policies, and intends to show the State Bar of California only appropriate investments.
- (g) **Service Provider Controls:** The State Bar shall annually obtain and review the System and Organization Controls (SOC1) reports of custodians and investment managers each year to ensure reliability of data and reports received.

### **Section 3    *Investment Instruments Authorized By The State Of California***

The following table identifies the investment instruments, maturities, portfolio percentage restrictions and other minimum quality requirements established under California Law.

<b>The State Bar of California Investment Policy Investment Instruments Authorized by the State of California</b>			
<b>INVESTMENT TYPE</b>	<b>MAXIMUM MATURITY</b>	<b>MAXIMUM SPECIFIED % OF PORTFOLIO</b>	<b>MINIMUM QUALITY REQUIREMENTS</b>
Local Agency Bonds	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
State Obligations— CA And Others	5 years	None	None
CA Local Agency Obligations	5 years	None	None
U.S Agency Obligations	5 years	None	None
Bankers' Acceptances	180 days	40%	None
Commercial Paper— Pooled Funds	270 days	40% of the agency's money	Highest letter and number rating by an NRSRO
Commercial Paper— Non-Pooled Funds	270 days	25% of the agency's money	Highest letter and number rating by an NRSRO
Negotiable Certificates of Deposit	5 years	30%	None
Non-negotiable Certificates of Deposit	5 years	None	None



Placement Service Deposits	5 years	30%	None
Placement Service Certificates of Deposit	5 years	30%	None
Repurchase Agreements	1 year	None	None
Reverse Repurchase Agreements and Securities Lending Agreements	92 days	20% of the base value of the portfolio	None
Medium-Term Notes	5 years	30%	"A" rating category or its equivalent or better
Mutual Funds And Money Market Mutual Funds	N/A	20%	Multiple
Collateralized Bank Deposits	5 years	None	None
Mortgage Pass-Through Securities	5 years	20%	"AA" rating category or its equivalent or better
County Pooled Investment Funds	N/A	None	None
Joint Powers Authority Pool	N/A	None	Multiple
Local Agency Investment Fund (LAIF)	N/A	None	None
Voluntary Investment Program Fund	N/A	None	None
Supranational Obligations	5 years	30%	"AA" rating category or its equivalent or better

#### ***Section 4    Reports Of Investment Activities***

The Chief Financial Officer will make quarterly reports to the Board of Trustees on the status of the State Bar's Investment portfolio. These reports shall include information as to the type of investment, the amount of money invested with various institutions, market value for securities with a maturity of more than 12 months, purchase and maturity dates, rate of interest, and statement of portfolio liquidity, as required by California state law.

#### ***Section 5    Ethics And Conflicts Of Interest***

Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution of the investment program, or which could impair their ability to make impartial investment decisions. Investment officials and employees shall disclose any financial interests as required by the Conflict of Interest Code for Designated Employees of The State Bar of California and the Conflict of Interest Code for the State Bar Board of Trustees. All persons authorized to place or approve investments shall report annually on Form 700 of the California Fair Political Practices Commission all required economic interests for that year.

#### ***Section 6    Required Review Of State Bar Investment Policy***

This investment policy shall be reviewed at least annually for the purpose of recommending needed changes and modifications. The Chair of the Finance and Planning Committee will be responsible for initiating the review.

(Source: Board of Governors' Resolutions, September 1996, June 2000, September 2000, May 2005; Planning and Budget Committee Resolution, November 19, 2015; Finance and Planning Committee Resolution, November 17, 2016.)