



TO: Business – Finance Committee
-Chairman Smith
- Commissioner Geisreiter

FROM: Marian Olin, Port Director

DATE: July 20, 2018

SUBJECT: Consider Development of Investment Policy

BACKGROUND

The Port District currently invests cash in the State of California Local Agency Investment Fund Account (LAIF). The state's mission is to prudently manage the LAIF program under the statutory authority granted by state law and consistent with the investment objectives of safety, liquidity and yield.

Information on LAIF's performance and the District's quarterly interest earned is appended as Attachment A. The District's total earned interest from LAIF for the four quarters ending 3/31/18 was \$95,299.

The Commission may want to consider adoption of an investment policy, which could increase interest earned by the District. As a special district government, the Port District must comply with laws governing the investment of public funds. CPA Wendy Cumming will be present at the committee meeting to discuss the District's options for potentially increasing interest income earned by contracting with an investment manager experienced in fixed income investments appropriate for a government entity.

While some entities can achieve earnings of 5% to 7% through adoption of a well-managed investment policy, expected returns for government entities are more likely to be in the 2% to 3% range. While this is not a significant increase over LAIF's current yields, an increase of just 1% on a \$5 million investment is \$50,000.

DISCUSSION TOPICS

Should the Commission consider adopting an investment policy?

Appended to this report as Attachment B are two sample policies provided by CPA Wendy Cumming. These are examples only, and would have to be modified to fit the District's goals, objectives and legal requirements.

If the committee recommends adoption of a policy, staff would work with CPA Cumming to develop a draft policy for review by the committee. If the committee recommends adoption, the policy would be presented to the full Commission for consideration.

If an investment policy is developed and adopted, how will a contract investment manager be selected?

The Port District can issue a Request for Proposals (RFP) seeking proposals from qualified firms. Qualified firms identified in the RFP process can then be interviewed by the Business-Finance Committee. If the committee recommends retaining the services of an investment manager, the contract would be presented to the full Commission for consideration.

What other options may be available to the Port District to improve its investment strategy / financial position?

In March 2018, I attended a CalPERS' workshop to learn more about the California Employers' Retiree Benefit Trust (CERBT) fund. The workshop discussed the benefits of prefunding employer Other Post-Employment Benefit (OPEB) liabilities. While the program does not reduce future costs, it can reduce liability on the balance sheet; improve an entity's bond rating; achieve a higher return and it's flexible – the employer decides if, when and how much to contribute and funds can be withdrawn to offset OPEB costs.

The Port District currently has \$175,000 set aside in its Public Employees' Medical & Hospital Care Act (PEMHCA) fund. This cash savings is intended to offset the District's OBEB liability, but is not Government Accounting Standards Board (GASB) compliant pre-funding and does not offset balance sheet liability.

The Commission may wish to consider investing some or all of the \$175,000 it has set aside in the PEMHCA fund by incorporating this option in to an investment policy or learning more about this program independent of a larger policy.

ATTACHMENTS

- A. Local Agency Investment Fund Remittance Advice
- B. Investment Policy Statement (DRAFT)



BETTY T. YEE

California State Controller

LOCAL AGENCY INVESTMENT FUND
REMITTANCE ADVICE

Agency Name

SANTA CRUZ PORT DISTRICT

Account Number

80-44-001

As of 07/13/2018, your Local Agency Investment Fund account has been directly credited with the interest earned on your deposits for the quarter ending 06/30/2018.

Earnings Ratio		.00005216919081336
Interest Rate		1.90%
Dollar Day Total	\$	823,936,526.00
Quarter End Principal Balance	\$	9,362,917.08
Quarterly Interest Earned	\$	42,984.10



**JOHN CHIANG
TREASURER
STATE OF CALIFORNIA**



PMIA Performance Report

Date	Daily Yield*	Quarter to Date Yield	Average Maturity (in days)
06/18/18	1.86	1.74	181
06/19/18	1.87	1.74	179
06/20/18	1.87	1.74	178
06/21/18	1.89	1.74	183
06/22/18	1.89	1.75	186
06/23/18	1.89	1.75	186
06/24/18	1.89	1.75	186
06/25/18	1.89	1.75	184
06/26/18	1.89	1.75	183
06/27/18	1.90	1.75	181
06/28/18	1.90	1.76	183
06/29/18	1.92	1.76	194
06/30/18	1.92	1.76	193
07/01/18	1.92	1.92	193
07/02/18	1.93	1.92	196
07/03/18	1.93	1.92	195
07/04/18	1.93	1.92	195
07/05/18	1.93	1.93	194
07/06/18	1.93	1.93	193
07/07/18	1.93	1.93	193
07/08/18	1.93	1.93	193
07/09/18	1.93	1.93	191
07/10/18	1.93	1.93	192
07/11/18	1.93	1.93	191
07/12/18	1.94	1.93	189
07/13/18	1.94	1.93	190
07/14/18	1.94	1.93	190
07/15/18	1.94	1.93	190
07/16/18	1.94	1.93	188
07/17/18	1.94	1.93	187
07/18/18	1.94	1.93	187

*Daily yield does not reflect capital gains or losses

[View Prior Month Daily Rates](#)

LAIF Performance Report

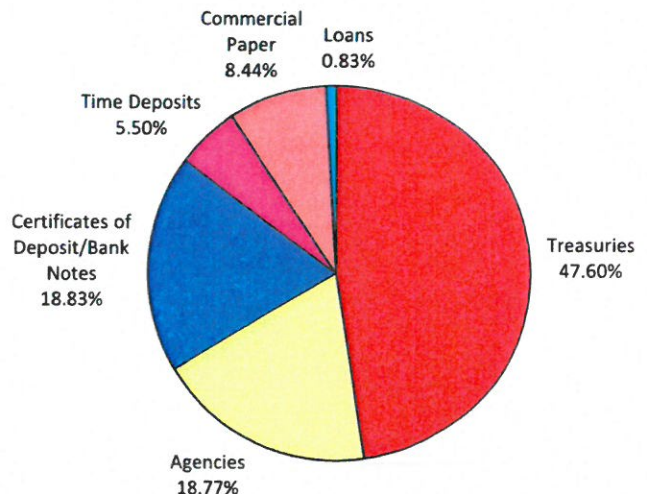
Quarter Ending 06/30/18

Apportionment Rate: 1.90%
 Earnings Ratio: 0.00005216919081336
 Fair Value Factor: 0.998126869
 Daily: 1.92%
 Quarter to Date: 1.76%
 Average Life: 193

**PMIA Average Monthly
Effective Yields**

June 2018 1.854
 May 2018 1.755
 Apr 2018 1.661

**Pooled Money Investment Account
Portfolio Composition
06/30/18
\$88.8 billion**



Based on data available as of 7/18/2018

Investment Policy Statement

The Entity

Draft for Review, Date

By Investment Committee

This investment policy statement should be reviewed and updated at least annually. Any change to this policy should be communicated in writing on a timely basis to all interested parties.

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DRAFT

I. BACKGROUND

The Entity is a legally constituted 501(c)3 non-profit organization

II. DUTIES AND RESPONSIBILITIES

Delegation of Authority

The Board of Directors are fiduciaries, and are responsible for directing and monitoring the investment management of Fund assets. As such, the Board is authorized to delegate certain responsibilities to the Investment Committee, and professional experts in various fields. These include, but are not limited to:

1. Investment Consultant. The investment consultant may assist the Committee in: Establishing investment policy, objectives, and guidelines; selecting investment options and managers; reviewing such options and managers over time; measuring and evaluating investment performance; and other tasks as deemed appropriate.
2. Investment Manager. The investment manager has discretion to purchase, sell, or hold the specific securities that will be used to meet the Fund's investment objectives.
3. Custodian. The custodian will physically (or through agreement with a sub-custodian) maintain possession of securities owned by the Fund, collect dividend and interest payments, redeem maturing securities, and effect receipt and delivery following purchases and sales. The custodian may also perform regular accounting of all assets owned, purchased, or sold, as well as movements of assets into and out of the Fund accounts.
4. Additional specialists such as attorneys, auditors, actuaries, and others may be employed by the Committee to assist in meeting its responsibilities and obligations to administer Fund assets prudently.

The Committee will not reserve any control over investment decisions, with the exception of specific limitations described in these statements. Investment managers will be held responsible and accountable to achieve the objectives herein stated. While it is not believed that the limitations will hamper investment managers, each manager should request modifications that they deem appropriate.

Comment [AKS1]: To reply to Bob's Comment 2, I don't think so.

Comment [RH2]: Can the "investment manager" be a mutual fund or an ETF? E.g. Dodge and Cox Stock Fund.

III. ASSIGNMENT OF RESPONSIBILITY

The Board of Directors has general charge of the affairs, property and assets of the Foundation Entity and is responsible for directing and monitoring the investment management of fund assets. As such, the Board is authorized to delegate certain responsibilities and may employ or arrange for the services of such other persons, agents or assistants as in its opinion are necessary or desirable for the proper administration of the Foundation Entity, and to pay reasonable compensation for their services and expenses

Comment [AKS3]: I want to rearrange this, because the Board does not have the obligation to diversify funds so as to avoid risk. We have the obligation to wisely pick the investment managers who will do that for us.

The Board expects that the following parties associated with the FoundationEntity will discharge their respective responsibilities in accordance with normal fiduciary standards: (1) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and of like aims, and (2) by diversifying the investments so as to minimize the risk of large losses.

- **Investment Manager(s)**

The Investment Manager(s) are charged with the responsibility to conduct day-to-day investment management of the FoundationEntity assets in accordance with this Investment Policy Statement and all laws that supplement, amend, modify or supersede it. All Investment Manager(s) must either be (1) registered under the Investment Company Act of 1940, (2) a bank, as defined in that Act, (3) an insurance company qualified under the laws of more than one state to perform the services of managing, acquiring or disposing of FoundationEntity assets, or (4) such other person or organization authorized by applicable law or regulation to function as an Investment Manager. Each Investment Manager managing a separate account for the FoundationEntity must sign an investment management agreement with the FoundationEntity.

Comment [RH4]: If a mutual fund or ETF is deemed to be a Investment Manager, is it possible that such an entity could sign an investment management agreement?

- **Custodian(s)**

The Custodian(s) has been retained by the Investment Committee and is charged with the responsibility for safekeeping securities, collections and disbursements, and providing periodic accounting statements.

- **Investment Committee**

Subject to approval by a majority of the Board, this committee is appointed annually by the Board Chair, and consists of a Chairperson who is a current member of the Board, and shall include the Treasurer and at least one (1) other Director. The Board Chair may appoint additional non-Directors who shall serve in an advisory capacity. This committee has the responsibility to provide the following services to the Board:

1. The Investment Committee will conduct annual reviews and monitoring of investment objectives, procedures, performance, practices and fees for all funds held and administered by the FoundationEntity. Performance will be measured and evaluated not less than quarterly relative to generally accepted benchmarks for each investment class or type.
2. The Investment Committee will recommend to the Board any changes to the IPS, including broad asset allocation policy and ranges.
- 3.2.
- 4.3. The Investment Committee will make recommendations to the Board on the employment of such investment professionals and investment managers as may be required from time to time, and on other matters involving administration of the FoundationEntity's assets.
- 5.4. The Investment Committee will recommend the annual payout rate to the Board, taking into account factors described in Section IV.
- 6.5. The Investment Committee will provide investment oversight of the FoundationEntity's funds.

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Comment [RH5]: I think we need Definitions Section to define terms like "annual payout rate".

Comment [AKS6]: I agree with Bob's comment.

- **Investment Consultant**

The Investment Consultant is charged with the responsibility to assist the Investment Committee with its supervision of the FoundationEntity's assets.

The Investment Consultant retained by the Board will assist the Investment Committee in from time-to-time reviewing and revising this IPS.

1. The Investment Consultant will monitor asset allocation across and among asset classes. Following the close of a quarter where the actual allocations fall outside the IPS ranges, the Investment Consultant will create directives to reallocate assets in accordance with the rebalance procedure described in Section V.
2. The Investment Consultant will monitor the investment performance of the FoundationEntity. Performance reports will be provided to the Investment Committee quarterly. The Investment Consultant will report in a timely manner any substantive developments that may affect the management of FoundationEntity assets.
3. The Investment consultant will conduct investment manager searches when requested by the committee, monitor the performance of the investment manager(s), and make recommendations on the retention or removal of a manager.
4. The Investment Consultant will be compensated on a fee for service basis only, where the fee will not be tied to investment performance, i.e. contingent fee arrangement.

IV. STATEMENT OF OBJECTIVES

In order to maintain the FoundationEntity in perpetuity and meet its needs, the Fund will employ a strategy that emphasizes a balanced return, relying on both current income and growth of principal (from capital appreciation, dividends, and interest income).

• General Investment Principles

1. Investments shall be made solely in the interest of the FoundationEntity.
2. The Fund shall be invested with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in like capacity and familiar with such matters would use in the investment of a fund of like character and with like aims.
3. Investment of the Fund shall be so diversified as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so.
4. The Committee may employ one or more investment managers of varying styles and philosophies to attain the Fund's objectives.

• Spending Policy

The Committee will apply a smoothing rule to mitigate the effects of short-term market volatility when calculating the level of annual spending.

Under the Uniform Prudent Management of Institutional Funds Act (UPMIFA), the appropriation rate of 7% of endowment balance will be applied to an average of the past three years of the portfolio's market values and these funds will be placed in a distributable fund.

The Committee will annually determine the amount to be spent from this distributable fund, based on the needs of the Organization.

Comment [RH7]: Same comment as above. Need definition of "level of annual spending".

- **Performance Expectations**

The desired investment objective is a long-term rate of return on assets that is at least 7.5% as measured against the overall change in the market for the same reporting timeframe. The short-term objective of rate of return on assets is 3% to 5% greater than the anticipated rate of inflation as measured by the Consumer Price Index San Francisco/Oakland/San Jose Consumer Price Index, All Urban Consumers. The target rate of return for the Fund has been based upon the assumption that future real returns will approximate forward looking asset class projections provided by the Consultant for each asset class in the IPS.

The Committee realizes market performance varies and a 7.5% rate of return may not be meaningful during some periods. Accordingly, relative performance benchmarks for the managers are set forth in the "Investment Manager Performance Review and Evaluation" section. Over a complete business cycle, the Fund's overall annualized total return, after deducting for advisory, money management, and custodial fees, as well as total transaction costs, should perform above a customized index comprised of market indices weighted by the strategic asset allocation of the Fund.

Comment [AKS8]: I like Bob's idea in his comment 17.

Comment [RH9]: Maybe it would be simpler to state that the desired rate of return is (e.g.) x% greater than the CPI. This gets rid of targeting a particular rate of return; e.g. "7.5%"

V. ASSET ALLOCATION GUIDELINES

Investment management of the assets of the Fund shall be in accordance with the asset allocation guidelines determined by the Investment Committee in consultation with the Investment Consultant. The following illustrates the format and the kinds of investments, and is provided as an example:

- Aggregate Fund Asset Allocation Guidelines (at market value)

Asset Class:	Min. Wt.	Max Wt.	Target Wt.
Equities:	40%	70%	55%
Large Cap	14%	34%	24%
Mid Cap	3%	23%	13%
Small Cap	0%	14%	4%
International	4%	24%	14%
Fixed Income:	17%	47%	31%
Taxable	5%	25%	14%
Specialty	7%	27%	17%
Alternatives:	0%	28%	11%
Specialty Equity	0%	28%	7%
Real Assets	0%	28%	4%
Cash & Equivalent:	0%	5%	3%

Comment [AKS10]: What is the source of these numbers and breakdowns?

- The Committee may employ investment managers whose investment disciplines require investment outside the established asset allocation guidelines. However, taken as a component of the aggregate Fund, such disciplines must fit within the overall asset allocation guidelines established in this statement. Such investment managers will receive written direction from the Committee regarding specific objectives and guidelines.

Comment [RH11]: I would like to have a situation where the Investment Consultant along with the Investment Committee (us), make specific asset allocations that are more tightly bounded than the above table for some time period. Then use the Investment Manager (maybe a mutual fund or ETF as well as an organization such as Todd Ganos) to execute this allocation at the least cost.

Rebalancing

The Consultant is expected to monitor the portfolio mix. Neither the upper nor the lower limits of the asset allocations are intended to require portfolio activity for the sole purpose of complying with the guidelines; however, deviation from these guidelines will be treated as discussion topics at the quarterly meetings with rebalancing considered at least annually. It is recommended that the target allocation be maintained so that the Fund will be able to achieve its long-term goals.

VI. INVESTMENT GUIDELINES

For the assets of the FoundationEntity which are invested in commingled funds, mutual funds and exchange traded funds the investment guidelines that govern the management of these respective accounts will be governed by the applicable governing document of the fund. No more than 10% of the assets of the FoundationEntity shall be invested in the securities of any one issuer, other than mutual funds, or any class of insurer, other than U.S. Government Bonds or regulated investment companies. No more than 10% of the overall fixed income portfolio shall be invested in non-investment grade debt. The FoundationEntity shall not buy securities on margin, or purchase futures, options and derivatives.

Conversion of Securities and Other Assets - The FoundationEntity's general practice is to sell securities as soon as they are donated to the FoundationEntity. Deviation from this general practice will be discussed with the Investment Advisor on a case-by-case basis and if the Investment Advisor recommends that the securities be held rather than sold, the Investment Committee is granted the discretion to retain the securities in the form as donated. The FoundationEntity's general practice is to sell real property, artifacts, and other illiquid assets as soon as reasonably possible after they are donated to the FoundationEntity, with expenses of sale to be borne by the fund or funds created with those assets.

Cash Management - The FoundationEntity maintains accounts with recognized banks for operating expenses. All cash receipts are recorded and deposited into these accounts, or other banks, money market funds, and/or the commingled investment fund. Specific cash management policies are promulgated by and are the responsibility of the FoundationEntity's Finance Committee.

VII. INVESTMENT PERFORMANCE REVIEW AND EVALUATION

The most important performance expectation is the achievement of long-term investment results that are consistent with the FoundationEntity's IPS. Implementation of the investment policy will be directed toward achieving this return and not toward maximizing return without regard to risk.

The Investment Committee recognizes that this return objective may not be attainable during some time periods. In order to ensure that investment opportunities available over a specific time period are fairly evaluated, comparative performance statistics (including benchmark indices) will be used to evaluate investment results. To that end, the Investment Committee will periodically review the investment results of the Investment Managers. Performance comparisons will be made against a representative performance universe and the performance objectives set forth in this IPS.

The Investment Committee with the assistance of the Investment Consultant shall also periodically review the qualitative developments of each Investment Manager. This evaluation shall include: changes in ownership, personnel turnover, adherence to investment style and philosophy, and any other qualities that the Investment Committee deems appropriate.

VII. INVESTMENT POLICY REVIEW

The Committee will review this IPS at least annually to determine whether stated investment objectives are still relevant and the continued feasibility of achieving the same. It is not expected that the IPS will change frequently. In particular, short-term changes in the financial markets should not require adjustments to the IPS.

This statement of investment policy is adopted on _____ (date) by the Committee whose signatures appear below.

Committee members

Approved:

Consultant:

Title: _____

Title: _____

Date

Date

DRAFT

GLOSSARY

The following is a glossary* of key terms, that appear in ESF's the Organization's Investment Policy.

Annual Payout Rate – The portion of the total returns on the portfolio that is allocated for use each year. This will be determined by the Investment Committee working with the Finance Committee and assessing the needs of the organization and the status of the investments.

Consumer Price Index (CPI) - measures changes in the price level of a market basket of consumer goods and services purchased by households. The CPI in the United States is defined by the Bureau of Labor Statistics as "a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. The annual percentage change in a CPI is used as a measure of inflation. For purposes of ESF the Organization's investments, we use the SAN FRANCISCO-OAKLAND-SAN JOSE Consumer Price Index, All Items, 1982-84=100 for All Urban Consumers (CPI-U)

Custodian - A custodian bank, or simply **custodian**, is a specialized financial institution responsible for safeguarding a firm's or individual's financial assets and is not necessarily engaged in "traditional" commercial or consumer/retail banking. The role of a custodian in such a case would be to:

- hold in safekeeping assets/securities such as stocks, bonds, commodities such as precious metals and currency (cash), domestic and foreign
- arrange settlement of any purchases and sales and deliveries in/out of such securities and currency
- collect information on and income from such assets (dividends in the case of stocks/equities and coupons (interest payments) in the case of bonds) and administer related tax withholding documents and foreign tax reclamation
- administer voluntary and involuntary corporate actions on securities held such as stock dividends, splits, business combinations (mergers), tender offers, bond calls, etc.
- provide information on the securities and their issuers such as annual general meetings and related proxies
- maintain currency/cash bank accounts, effect deposits and withdrawals and manage other cash transactions
- perform foreign exchange transactions
- often perform additional services for particular clients such as mutual funds; examples include fund accounting, administration, legal, compliance and tax support services

For the OrganizationESF, examples of Custodians are Schwab and Wells Fargo Bank.

Diversification - A process of investing assets among a range of security types by sector, maturity,

and quality rating.

Fiduciary - A **fiduciary** is a legal or ethical relationship of trust between two or more parties. Typically, a fiduciary prudently takes care of money for another person. One party, for example a corporate trust company or the trust department of a bank, acts in a fiduciary capacity to the other one, who for example has entrusted funds to the fiduciary for safekeeping or investment. Likewise, asset managers--including managers of pension plans, endowments and other tax-exempt assets--are considered fiduciaries under applicable statutes and laws.[1] In a fiduciary relationship, one person, in a position of vulnerability, justifiably vests confidence, good faith, reliance and trust in another whose aid, advice or protection is sought in some matter. In such a relation good conscience requires the fiduciary to act at all times for the sole benefit and interest of the one who trusts.

Investment Company Act of 1940 - Federal legislation which sets the standards by which investment companies, such as mutual funds, are regulated in the areas of advertising, promotion, performance reporting requirements, and securities valuations.

Investment Consultant – Independent agent or firm that works on behalf of the committee and board to develop asset allocations consistent with the organizations goals, provides information on managers, recommends Investment Managers, Evaluates manager performance and recommends to the committee manager retention or termination. The committee is responsible for selection and termination of managers.

Investment Manager - the entity, whether an individual, bank trust department, mutual fund organization or independent investment-advisory firm, that selects the investment instruments to meet the goals and guidelines established by the investor, in this case, the OrganizationESF.

Investment Policy - A concise and clear statement of the objectives and parameters formulated by an investor or investment manager to manage a portfolio of investment securities.

Money Market Mutual Funds - Mutual funds that invest solely in money market instruments (short-term debt instruments, such as Treasury bills, commercial paper, bankers' acceptances, repos and federal funds).

Mutual Fund – Pooled money that an investment company invests in a variety of securities, including fixed-income securities and money market instruments.

Prudent Person Rule - An investment standard outlining the fiduciary responsibilities of public funds investors relating to investment practices.

Total Return - The sum of all investment income plus changes in the capital value of the portfolio. For mutual funds, return on an investment is composed of share price appreciation plus any realized dividends or capital gains. $(\text{Price appreciation}) + (\text{Dividends paid}) + (\text{Capital gains}) = \text{Total Return}$

UPMIFA - the Uniform Prudent Management of Institutional Funds Act provides guidance on investment decisions and endowment expenditures for nonprofit and charitable organizations. As of October 2010, UPMIFA is now the law in the District of Columbia and all states except Pennsylvania, Florida and Mississippi. The major change in UPMIFA compared to the previous model law (the Uniform Management of Institutional Funds Act) is that it replaces a requirement that nonprofits cannot spend below the original value of contributions or "historic dollar value" (HDV) with a new requirement that their investing and spending will be at a rate that will preserve the purchasing power of the principal over the long term.

[ENTITY]

**STATEMENT OF
INVESTMENT POLICY**

2017 - 2018

PREPARED BY THE CITY FINANCE DEPARTMENT

REVIEWED AND APPROVED BY

[Name]

Adopted by the City Council on TBD

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I. OVERVIEW

Introduction

The purpose of this document is to provide guidelines for the prudent investment of the City's idle cash and to outline policies for investment transactions. The ultimate goal is to enhance the economic status of the City while protecting its pooled cash.

Scope

The scope of the City's investment policy includes the criteria and practices to be followed in the process of realizing the City's primary investment objectives for the following categories:

- Authority and Responsibilities
- Eligible Financial Institutions
- Authorized Investments
- Investment Parameters
- Cash Management
- Evaluation of Investment Performance
- Investment Reporting
- Investment Policy Review and Adoption

This policy covers all funds and investment activities which are under direct authority of the City and accounted for in the Annual Financial Report.

Financial assets held and invested by trustees or fiscal agents are excluded from this policy, however, such assets are nevertheless subject to and governed according to the regulations established by the State of California pertaining to investments by local agencies as well as the relative bond indentures.

General Objectives

In order of priority, the primary objectives of investment activities shall be:

1. Safety

Safety of principal is the foremost objective of the investment program. Investments will be made in a manner that ensures the preservation of capital in the overall portfolio. The objective is to mitigate credit and interest rate risk.

a. Credit Risk

The City will minimize credit risk, which is defined as the risk of loss due to the failure of the security issuer or backer, by:

- Limiting investments to the safest types of securities and investments as outlined in Section IV.
- Evaluating the financial stability, of the financial institutions, broker/dealer with which the City will do business.
- Diversifying the investment portfolio so that potential losses on individual securities will be minimized.

b. Interest Rate Risk

The City will minimize the fluctuations or market value risk of securities due to changes in general interest rates by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity.

2. Liquidity

The investment portfolio will remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by structuring the portfolio so that securities mature concurrent with cash needs to meet anticipated demands (static liquidity). Furthermore, since all possible cash demands cannot be anticipated, the portfolio will consist largely of securities with an active secondary or resale market (dynamic liquidity). A portion of the portfolio will also be placed in money market mutual funds or local government investment pools, which offer same-day or next day liquidity for short-term funds.

3. Yield

The investment portfolio is designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, while taking into account investment risk constraints and liquidity needs. Return on investment is secondary to safety and liquidity objectives. The core of investments is limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed. It is the City's policy to hold investments to maturity; however, securities may be sold prior to maturity under the following circumstances:

- When a security has declining credit and selling early will minimize loss of principal.
- When a security swap will improve the quality, yield, or target duration in the portfolio.
- When liquidity needs of the portfolio cause the security to be sold.

Standards of Care

The City operates its pooled idle cash investments under the "Prudent Person Rule" which obligates a fiduciary to ensure that:

"In investing...property for the benefit of another, a trustee shall exercise the judgment and care, under the circumstances then prevailing, which men or women of prudence, discretion and intelligence exercise in the management of their own affairs."

II. INVESTMENT AUTHORITY AND RESPONSIBILITIES

Authorized Investment Officers

Idle cash management and investment transactions are the responsibility of the City Treasurer.

Investment Procedures

The authorized investment officers, in accordance with the City of Entity Investment Policy, are responsible for administering an investment program which:

- Adheres to the Statement of Investment Policy.
- Prioritizes safety and liquidity.
- Determines risk and optimizes return.
- Meets anticipated cash needs.

III. ELIGIBLE FINANCIAL INSTITUTIONS

Selection of Eligible Financial Institutions

All financial institutions and broker/dealers who desire to become qualified for investment transactions must supply the following as appropriate:

- Audited financial statements.
- Proof of National Association of Securities Dealers (NASD) certification.
- Proof of state registration.
- Completed broker/dealer questionnaire.
- Certification of having read, understood, and agreed to comply with the City's investment policy.

Deposits

The City will only deposit funds with institutions that have been assigned an "A" rating by an established rating service that bases ratings on quarterly financial information provided by the Federal Reserve Board and the Federal Home Loan Bank Board (i.e., The Financial Directory). Ratings will be monitored on a quarterly basis.

Broker/Dealers

Investments must be purchased directly from the issuer, from an institution licensed by the state as a broker-dealer, from a member of a federally regulated securities exchange, or from a brokerage firm designated as a primary government dealer by the Federal Reserve Bank. Broker/dealers shall be selected according to creditworthiness (e.g., a minimum capital requirement of \$10,000,000 and at least five years of operation). Broker/Dealers may be either primary dealers or regional dealers that qualify under Securities and Exchange Commission Rule 15c3-1 (uniform net capital rule).

The City of Entity will maintain a file of broker/dealers with which it is currently doing business to include the firm name, contact person, telephone number, and current audited financial statements.

Safekeeping and Custody

When applicable, all trades will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible financial institution prior to the release of funds. A third-party custodian as evidenced by safekeeping receipts will hold securities.

IV. AUTHORIZED INVESTMENTS**Investment Types**

The California Government Code Sections 16429.1 and 53601 govern investment of City funds. Investments are restricted to a maturity term no longer than what is authorized by Section 53601, or five years unless the City Council grants prior express authority.

It should be noted that while the Government Code specifies the maximum percentage of the portfolio, which may be held in each type of investment at any one time, fluctuations in the portfolio balance prevents strict adherence to such restrictions. Therefore, percentage limitations shall apply to investments at the time of purchase.

Consistent with the GFOA Policy Statement on State and Local Laws Concerning Investment Practices, the following investments will be permitted by this policy:

1. State Treasurer's Local Agency Investment Fund (LAIF)

Government Code Section 16429.1: The City may invest a maximum of \$50 million pursuant to LAIF policy. LAIF is a diversified investment pool administered by the California State Treasurer. Monies invested with LAIF are pooled with State monies in order to earn the maximum rate of return consistent with safe and prudent treasury management.

The LAIF handbook including LAIF policies and restrictions shall be available in the City's Finance Department.

2. U.S. Government Issues

Government Code Sections 53601 (b) and (e): The California Government Code does not legislate a maximum for government issues. U.S. government agency obligations and U.S. government instrumentality obligations have a liquid market with a readily determinable market value. The State Code restricts the maturity limits for government obligations for Cities in California to a maximum of five years unless the legislative body has granted express authority to make an individual investment either specifically or as part of an investment program approved by the legislative body no less than three months prior.

3. Bankers Acceptances

Government Code Section 53601 (f): Up to forty percent (40%) of the City's portfolio may be invested in Bankers Acceptances which are defined as bills of exchange or time drafts, drawn on and accepted by a commercial bank, which are eligible for purchase by the Federal Reserve System. No more than 30% of the portfolio may be invested in Bankers Acceptances with any one commercial bank and the maturity periods cannot

exceed 180 days.

4. Commercial Paper

Government Code Section 53635 (a) & 53601 (g): A maximum of forty (40%) of the City's portfolio may be invested in commercial paper that is rated "A" or higher by a nationally recognized statistical-rating organization (NRSRO). Issuing corporations must be organized and operating in the United States, have \$500 million in total assets, and have at least an "A" rating (by a nationally recognized statistical-rating organization) on debt other than commercial paper. The maturity period cannot exceed 270 days. No more than 10% of the total investments held by a local agency may be invested in any one issuer's commercial paper.

5. Certificates of Deposit and Passbook Savings Accounts

Government Code Section 53601: There is no limit as to the amount of the investment portfolio that may be deposited in certificates of deposit or passbook savings account.

California law requires that public funds be collateralized. The depository must secure its public fund accounts by maintaining at least one hundred ten percent (110%) of the value of the public fund accounts. If a depository uses mortgage-backed securities (i.e., promissory notes secured by first mortgages or first deeds of trust) as collateral for public deposits, the market value of the mortgage-backed securities must be at least one hundred fifty percent (150%) of the value of the public fund accounts. Certificates of Deposit maturities cannot exceed 5 years.

The collateralization requirement may be waived if funds are federally insured (currently up to \$100,000 per institution). For deposits equivalent to the maximum insured amount, security may also be waived for interest accrued on the deposit provided the interest is computed by the depository on the average daily balance of the deposits, paid monthly, and computed on a 360-day basis.

6. Money Market Mutual Funds

Government Code Section 53601 (k): Money market funds that are shares of beneficial interest issued by diversified management companies registered with the Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. Sec 80a-1 et seq.) No more than 10% of the local agency's funds may be invested in shares of beneficial interest of any one mutual fund.

An investment in shares issued pursuant to the previous paragraph requires that the company shall have met either of the following criteria:

- a) Attained the highest ranking or the highest letter and numerical rating provided by not less than two nationally recognized statistical rating organizations.
- b) Retained an investment adviser who is registered or exempt from registration with the Securities and Exchange Commission, has at least five years experience managing money market mutual funds with assets in excess of five hundred million dollars (\$500,000,000).

The purchase price of shares of beneficial interest purchased pursuant to this section shall not include any commission that the companies may charge and shall not exceed twenty percent

(20%) of the agency's surplus money that may be invested pursuant to this section.

7. Medium Term Notes

Government Code Section 53601 (j): Medium-term notes with a maximum five year maturity issued by corporations organized and operating within the United States, or by depository institutions licensed by the United States or any individual state and operating within the United States. Notes eligible for investment under this section shall be rated in a rating category of "A", or its equivalent or better, by a nationally recognized rating service. Purchases of medium-term notes may be exceed thirty percent (30%) percent of the agency's surplus money, which may be invested pursuant to this section.

8. Negotiable Certificates of Deposit

Government Code Section 53601 (h): Negotiable certificates of deposits issued by a nationally or state-chartered bank, or a state of federal associations (as defined by Section 5102 of the Financial Code), or by a state-licensed branch of a foreign bank. Purchases of negotiable certificates of deposit may not exceed thirty percent (30%) of the agency's surplus money, which may be invested pursuant to this section. For purposes of this section, negotiable certificates of deposit are not subject to Article 2 requirements commencing with Section 53630, except that the amount so invested shall be subject to the limitations of 53638.

9. Repurchase Agreements

Government Code Section 53601 (i.2): Investments in repurchase agreements may be made, on any investment authorized in this section, when the term of the agreement does not exceed one year. The market value of securities that underlay a repurchase agreement shall be valued at a minimum of 102 percent of the funds borrowed against those securities and the value shall be adjusted no less than quarterly.

Prohibited Investments

The City of Entity shall not invest in any investment instrument/pool/fund unless it is specifically allowed under the "Investment Types" section of this policy.

The City of Entity shall comply with Government Code Section 53601.6, which states "A local agency shall not invest any funds pursuant to this article or pursuant to Article 2 (commencing with Section 53630) in inverse floaters, range notes, or mortgage-derived, interest-only. A local agency shall not invest any funds pursuant to this article or pursuant to Article 2 (commencing with Section 53630) in any security that could result in zero interest accrual if held to maturity."

In addition, the City of Entity will not invest in:

- Financial Futures and Financial Options.
- Guaranteed Small Business Administration (SBA) Notes.
- Reverse Repurchase Agreements.
- County Pooled Funds.

Legislative Changes

Any State of California legislative action that further restricts allowable maturities, investment types, or percentage allocations will be incorporated into the City of Entity Investment Policy. If the City is holding an investment that is subsequently prohibited by a legislative change, the City may hold that investment until the maturity date to avoid an unnecessary loss if it is deemed prudent to do so.

V. INVESTMENT PARAMETERS

Diversification

The investments shall be diversified by:

- Limiting investments in securities from a specific issuer or business sector (excluding Local Agency Investment Fund and U.S. Treasury securities) in order to avoid over concentration.
- Limiting investment in securities that have high credit risks.
- Investing in securities with varying maturities.
- Continuously investing a portion of the portfolio in readily available funds such as local government investment pools (LAIF) or money market funds in order to ensure that appropriate liquidity is maintained to meet ongoing obligations.

Maximum Maturities

In order to minimize the impact of market risk, it is intended that all investments will be held to maturity.

The City shall attempt to match its investments with anticipated cash flow requirements. The City will not directly invest in securities maturing more than five (5) years from the date of purchase.

Investments may be sold prior to maturity for cash flow or appreciation purposes, or in order to limit losses.

Because of inherent difficulties in accurately forecasting cash flow requirements, a portion of the portfolio should be continuously invested in readily available funds.

VI. CASH MANAGEMENT

In order to obtain a reasonable return on public funds, the following cash management practice will be followed:

- Maximum investment of all City funds not required to meet immediate cash flow

needs will be maintained.

- Except for cash in certain restricted and special funds, the City will consolidate cash balances from all funds to maximize investment earnings. Investment income will be allocated to the various funds on a quarterly basis based on participation and in accordance with generally accepted accounting principles.
- The City's cash flow will be maximized through immediate deposit of all receipts, use of direct deposit when available, and appropriate timing of payment to vendors.

VII. EVALUATION OF INVESTMENT PERFORMANCE

The investment portfolio will be designed to obtain a market average rate of return during budgetary and economic cycles, taking into account the City's investment risk constraints and cash flow needs.

Benchmark Comparison

The investment portfolio shall be structured to optimize the return given the risk constraints and cash flow needs.

In evaluation of the performance of the City's portfolio and compliance with this policy, it is expected that yields on City investments will regularly meet or exceed the average return on a two-year U.S. Treasury Note, however, a variance of .5% positive or negative from the benchmark is considered reasonable.

VIII. INVESTMENT REPORTING

Investment performance statistics and activity reports shall be generated on a monthly basis. The City Treasurer shall prepare and submit a monthly investment report to the City Manager for distribution to the City Council.

This report will include the following elements relative to the investments held at month-end.

- Par value.
- Security description.
- Coupon rate.
- Maturity date.
- Investment type.
- Purchase date.
- Cost of security.

- Purchase yield.
- Estimated market value.
- Statement of portfolio compliance with Investment Policy.
- Statement of sufficient funds to meet the next six months' obligations.

IX. INVESTMENT POLICY REVIEW AND ADOPTION

The Statement of Investment Policy shall be submitted annually to the City Council for adoption. The policy shall be reviewed at least annually to ensure its consistency with the overall objectives of the City and its relevance to current law and financial and economic trends. Any modifications made thereto must be approved by the City Council.

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APPENDIX A

DEPOSITORY SERVICES

Active Deposits are demand or checking accounts, which receive revenues and pay disbursements.

Interest-Bearing Active Deposits are money market accounts at a financial institution (i.e., bank, savings and loan, credit union). These accounts are demand accounts (i.e., checking accounts) with restricted transaction activity.

Inactive Deposits are certificates of deposit issued in any amount for periods of time as short as 14 days and as long as several years. Interest must be calculated on a 360-day basis, actual number of days.

Passbook Savings Account is similar to an inactive deposit except there is not a fixed term. The interest rate is much lower than CD's but the savings account allows greater flexibility as funds can be deposited and withdrawn according to our daily needs.

INVESTMENT SECURITIES

U.S. Treasury Issues are direct obligations of the United States Government. These issues are called bills, notes, and bonds. The maturity range of new issues is from 13 weeks (T-bills) to 30-year (T-bonds). These are highly liquid and considered the safest investment security.

Federal Agency Securities are issued by U.S. Government agencies or quasi- government agencies and are guaranteed either directly or indirectly by the United States Government. Federal Home Loan Bank (FHLB) notes, Federal National Mortgage Association (FNMA) notes, Federal Farm Credit Bank (FFCB) notes, Federal Intermediate Credit Bank (FICB) debentures, Small Business Administration (SBA) notes (as a matter of policy the City of Entity does NOT invest in SBA notes), Government National Mortgage Association (GNMA) notes, Federal Home Loan Mortgage Corporation (FHLMC) notes, and Student Loan Association (SALLIEMAE) notes are examples of these securities.

Certificates of Deposit are investments for inactive funds issued by banks, savings and loans, and credit unions. Investments up to \$100,000 are insured by the Federal Deposit Insurance Corporation (FDIC), Savings Association Insurance Fund (SAIF) which is managed by the FDIC, or the National Credit Union Share Insurance Fund (NCUSIF) according to issuance. Certificates of Deposit can be issued for a maturity period of 14 days to several years which allows for better matching of investments to cash flow needs. For deposits exceeding \$100,000, it is required that the financial institution collateralize with 110% government securities collateral, 150% First Trust Deeds collateral, or 105% Letters of Credit (L.C.) collateral.

Negotiable Certificates of Deposit are unsecured obligations of the financial institution. These securities are generally issued in bearer form and pay interest at maturity. Although negotiable, a strong secondary market exists only in the NCD's issued by the largest United States banks such as Bank of America, Citibank, Chase Manhattan, Manufacturers Hanover, etc.

Bankers Acceptances are short-term credit arrangements to enable businesses to obtain funds to finance commercial transactions. They are time drafts drawn on a bank by an exporter or importer to obtain funds to pay for specific merchandise. By its acceptance, the bank becomes primarily liable for the payment of the draft at maturity. An acceptance is a high-grade negotiable instrument and is purchased in various denominations for 30, 60, 90, or 180 days. The interest is calculated on a 360-day discount basis similar to Treasury Bills. Local agencies cannot invest more than 40% of their surplus money in banker's acceptances.

Commercial Paper is a short-term unsecured promissory note issued by a corporation to raise working capital. These negotiable instruments are purchased at a discount but mature at par value. Commercial paper is issued by corporations such as General Motors Acceptance Corporation (GMAC), Shearson-American Express, Bank of America, Wells Fargo Bank, etc.

Local agencies are permitted by state law to invest in commercial paper of "prime" quality of the highest ranking, or of the highest letter and numerical rating as provided by Moody's Investor's Service, Inc., or Standard and Poor's Corporation. Purchases of eligible commercial paper may not exceed 270 days maturity nor exceed 25% of the local agency's surplus funds.

Medium Term Corporate Notes are unsecured promissory notes issued by a corporation operating in the United States. These are negotiable instruments and are actively traded in the secondary market. Medium Term Corporate Notes (MTN) can be defined as extended maturity commercial paper. Corporations such as General Electric, GMAC, Citibank, and Wells Fargo Bank use MTN's to raise capital.

Local agencies are restricted by the Government Code to investments in corporations that are rated in a rating category of "A" or its equivalent or better by a nationally recognized rating service. Further restrictions are a maximum term of five years to maturity and total investments in Medium Term Corporate Notes may not exceed 30% of the local agency's surplus money.

Repurchase Agreements and Reverse Repurchase Agreements are short-term investment transactions. Banks buy temporarily idle funds from a customer by selling U.S. Government or other securities with a contractual agreement to repurchase the same securities on a future date. Repurchase agreements are typically for one to ten days in maturity. The customer receives interest from the bank. The interest rate reflects both the prevailing demand for Federal Funds and the maturity of the REPO. Some banks will execute repurchase agreements for a minimum of \$100,000, but most banks have a minimum of \$500,000. Investment in repurchase agreements may be made only if the term of the agreement does not exceed one year and if it is collateralized at a minimum of 102 percent.

A reverse-repurchase agreement (reverse-repo) is exactly what the name implies, which is borrowing to increase the rate of return on investments-also known as leveraging. The agency

invests periodically in repurchase agreements, but as a matter of policy the City of Entity does NOT invest in reverse-repurchasing agreements.

Local Agency Investment Fund (L.A.I.F.) is a special fund in the State Treasury that local agencies may use to deposit funds for investment. There is no minimum investment period and the minimum transaction is \$5,000, and in multiples of \$1,000 above that, with a maximum of \$50 million for any agency. It offers high liquidity because deposits can be converted to cash in 24 hours and no interest is lost. All interest is distributed to those agencies participating on a proportionate share determined by the amounts deposited and the length of time they are deposited. Interest is paid quarterly via check, warrant, or direct deposit to the agency's State Pooled Fund account.

The State keeps an amount not to exceed 1/2 of a percent of the earnings for reasonable costs of making the investments.

County Pooled Funds is similar to the State of California Local Agency Investment Fund (L.A.I.F.). The County Treasurer manages this pooled fund and interest is competitive with money market rates. There are no restrictions regarding the number of transactions or dollar amount of deposits. The County cannot attach the funds deposited by a local agency in the County Pooled Fund.

All interest is distributed to the participating agencies on a proportionate share basis which is determined according to the amount deposited and the time length of the deposit. Interest is paid quarterly via check, warrant or direct deposit to the agency's County Pooled Fund account. The County keeps an amount for reasonable administrative costs. The Orange County Investment Pool is excluded from the City of Entity's allowable investment list.

Mutual Funds are referred to in the Government Code, Section 53601 as "shares of beneficial interest issued by diversified management companies." The Mutual Fund by-laws must be consistent with Government Code which allows Treasury issues, Federal Agency issues, State of California and city (within California) debt obligations, Bankers Acceptances, Commercial Paper, Certificates of Deposit, Negotiable Certificates of Deposit, Repurchase Agreements, Reverse Repurchase Agreements, Financial Futures and Financial Options and Medium Term Corporate Notes. The purchase price of shares of the mutual funds shall not include any sales commission and investments in mutual funds shall not exceed 20% of the local agency's surplus money. Companies in this category must have the highest rating provided by not less than two of the three largest nationally recognized rating services.

Financial Futures and Financial Options are forward contracts for securities. The Government Code States that a local agency may incur future contracts/options in any of the investment securities enumerated in Section 53601, a-m. Due to the volatility of trading in financial futures, the City of Entity does NOT invest in financial futures or financial options.

Derivatives are financial contracts that derive their value from some underlying asset such as mortgages, commodities, or stocks and bonds. Financial derivative products are more risky than other types of investments due to their complexity and the volatility of their market values. State

Legislation has limited this type of investment for local agencies by excluding the more risky derivatives. As a matter of policy, the City of Entity does NOT invest in derivative-type investments that do NOT conform to the requirements set forth in California Government Code Section 53635.

Money Market Funds are shares of beneficial interest issued by diversified management companies that are registered with the Securities and Exchange Commission. Money market funds are only authorized to invest in highly-rated, short-term debt instruments with defined maturities. They must have an average weighted maturity of 90 days or less and abide by SEC regulations. Only money market funds holding U.S. Treasury or government agency obligations are to be utilized. Funds must receive the highest ranking by 2 of the 3 largest nationally recognized rating agencies.

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APPENDIX B

INVESTMENT CRITERIA FOR FINANCIAL INSTITUTIONS

- The institution must have been in business for at least three years.
- The institution must submit audited financial statements.
- The institution must have assets of at least \$50 million and a net worth to liability ratio of 3.5% to 1 or 3.0% to 1 net worth to asset ratio if less than 180 days to maturity.
- Investments in Credit Unions require Equity (net worth) to Asset Value of 5.0%. The loan balance to share draft ratio is comparable to industry standards, but should not exceed 90%. The City may invest funds for a period of up to 120 days in institutions with a Regular Reserve to Loan Balance ratio of at least 3.25%. For longer periods of time, the ratio must be at least 4.0%.
- The institution will certify as to the adequacy of the Reserve Loan Losses category and to the level of non-performing assets (i.e., loans no longer paying interest and/or principal in the amount called for in the original contract agreement). Comparison is made of institution ratio values to the industry averages.
- Under deposits, if data is available, we will request information regarding the ratio of \$100,000 certificates of deposit (brokered money) to the total deposit base. A percent greater than 50% is an area of concern.

EXHIBIT A

BROKER/DEALER QUESTIONNAIRE

1. Name of Firm:
2. Local Address: National Address:
3. Telephone:
4. PRIMARY REPRESENTATIVE/MANAGER/PARTNER-IN-CHARGE:
Secondary representative/manager/partner-in-charge:
5. Are you a Primary Dealer in U.S. Government Securities?
6. Are you a member of NASD?
7. What is the date of your firm's fiscal year-end?
8. Attach certified documentation of your capital adequacy and financial solvency. In addition, an audited financial statement must be provided within 120 days of your fiscal year-end.
9. Has your Firm consistently complied with the Federal Reserve Bank's Capital adequacy guidelines?
10. Is your firm owned by a holding company? If so, what is its name and net capitalization?
11. Identify the principal who will be trading with or quoting securities to our employees (attach current resumes of all persons listed).
12. Please identify your most directly comparable clients in our geographical area. (include address, contact phone #, length of relationship)
13. Please indicate a percentage breakdown of your client base by portfolio size.

14. Have any of your public-sector clients ever sustained or claimed a loss on a securities transaction or loss of principal arising from a misunderstanding or misrepresentation of the risk characteristics of a recommended instrument purchased through your firm? If yes, please explain.
15. Does your firm have any pending litigation with public sector clients or have you been subject to any within the last five years? If yes, please explain.
16. Has your firm ever been subject to a regulatory, state, or federal agency investigation for alleged improper, fraudulent, disreputable or unfair activities related to the sale of government securities or money market instruments? If yes, please explain.
17. Please provide your wiring and delivery instructions.
18. Which instruments does your local desk offer regularly?
19. Which of the above does your firm specialize in marketing?
20. What reports, transaction confirmations, and paper trail will we receive?
21. What precautions are taken by your firm to protect the interest of the public when dealing with government agencies as investors?
22. What training would you provide for your employees and investment officers?
23. Do you participate in the SIPC Insurance program? If not, please explain.
24. What portfolio information do you prefer from your clients?
25. Please include samples of research reports or market information that your firm regularly provides to clients.
26. Are you, or is your institution, licensed by the State of California as a broker-dealer, as defined in Section 25004 of the California Corporations Code, or a member of a federally-regulated securities exchange, from a national or state-chartered bank, from a savings association or federal association (as defined by Section 5102 of the California Finance Code) or from a brokerage firm designated as a primary government dealer by the Federal Reserve Bank?

APPENDIX C GLOSSARY

The following is a glossary* of key investing terms, many of which appear in GFOA'S Sample Investment Policy.

Accrued Interest - The accumulated interest due on a bond as of the last interest payment made by the issuer.

Agency - A debt security that is issued by a federal or federally sponsored agency. Federal agencies are backed by the full faith and credit of the U.S. Government. Federally sponsored agencies (FSAs) are backed by each particular agency with a market perception that there is an implicit government guarantee. An example of a federal agency is the Government National Mortgage Association (GNMA). An example of an FSA is the Federal National Mortgage Association (FNMA).

Amortization - The systematic reduction of the amount owed on a debt issue through periodic payments of principal.

Average Life - The average length of time that an issue of serial bonds and/or term bonds with a mandatory sinking fund feature is expected to be outstanding.

Basis Point - A unit of measurement used in the valuation of fixed-income securities equal to 1/100 of 1 percent of yield, for example 1/4 of 1 percent is equal to 25 basis points.

Bid - The indicated price at which a buyer is willing to purchase a security or commodity.

Book Value - The value at which a security is carried on the inventory lists or other financial records of an investor. The book value may differ significantly from the security's current value in the market.

Callable Bond - A bond issue in which all or part of its outstanding principal amount may be redeemed before maturity by the issuer under specified conditions.

Call Price - The price at which an issuer may redeem a bond prior to maturity. The price is usually at a slight premium to the bond's original issue price to compensate the holder for loss of income and ownership.

Call Risk - The risk to a bondholder that a bond may be redeemed prior to maturity.

Cash Sale/Purchase - A transaction which calls for delivery and payment of securities on the same day that the transaction is initiated.

Collateralization - Process by which a borrower pledges securities, property, or other deposits

for the purpose of securing the repayment of a loan and/or security.

Commercial Paper - An unsecured short-term promissory note issued by corporations, with maturities ranging from 2 to 365 days.

Convexity - A measure of a bond's price sensitivity to changing interest rates. A high convexity indicates greater sensitivity of a bond's price to interest rate changes.

Coupon Rate - The annual rate of interest received by an investor from the issuer of certain types of fixed-income securities, also known as the "interest rate".

Credit Quality - The measurement of the financial strength of a bond issuer. This measurement helps an investor to understand an issuer's ability to make timely interest payments and repay the loan principal upon maturity. Generally, the higher the credit quality of a bond issuer, the lower the interest rate paid by the issuer because the risk of default is lower. Credit quality ratings are provided by nationally recognized rating agencies.

Credit Risk - The risk to an investor that an issuer will default in the payment of interest and/or principal on a security.

Current Yield (Current Return) - A yield calculation determined by dividing the annual interest received on a security by the current market price of that security.

Delivery Versus Payment (DVP) - A type of securities transaction in which the purchaser pays for the securities when they are delivered either to the purchaser or his/her custodian.

Derivative Security - Financial instrument created from, or whose value depends upon, one or more underlying assets or indexes of asset values.

Discount - The amount by which the par value of a security exceeds the price paid for the security.

Diversification - A process of investing assets among a range of security types by sector, maturity, and quality rating.

Duration - A measure of the timing of the cash flows, such as the interest payments and the principal repayment, to be received from a given fixed-income security. This calculation is based on three variables: term to maturity, coupon rate, and yield to maturity. The duration of a security is a useful indicator of its price volatility for given changes in interest rates.

Fair Value - The amount at which an investment could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

Federal Funds (Fed Funds) - Funds placed in Federal Reserve banks by depository institutions in excess of current reserve requirements. These depository institutions may lend fed funds to each other overnight or on a longer basis. They may also transfer funds among each other on a same-day basis through the Federal Reserve banking system. Fed funds are considered to be immediately available funds.

Federal Funds Rate - Interest rate charged by one institution lending federal funds to the other.

Government Securities - An obligation of the U.S. government, backed by the full faith and credit of the government. These securities are regarded as the highest quality of investment securities available in the U.S. securities market. See "Treasury Bills, Notes, and Bonds."

Interest Rate - See "Coupon Rate".

Interest Rate Risk - The risk associated with declines or rises in interest rates which cause an investment in a fixed-income security to increase or decrease in value.

Internal Controls - A structure designed to ensure that the assets of the entity are protected from loss, theft, or misuse. The concept of reasonable assurance recognizes that 1) the cost of a control should not exceed the benefits likely to be derived and 2) the valuation of costs and benefits requires estimates and judgments by management. Internal controls should address the following points:

- Control of collusion - Collusion is a situation where two or more employees are working in conjunction to defraud their employers.
- Separation of transaction authority from accounting and record keeping - By separating the person who authorizes or performs the transaction from the people who record or otherwise account for the transaction, a separation of duties is achieved.
- Custodial safekeeping - Securities purchased from any bank or dealer including appropriate collateral (as defined by state law) shall be placed with an independent third party for custodial safekeeping.
- Avoidance of physical delivery securities - Book-entry securities are much easier to transfer and account for since actual delivery of a document never takes place. Delivered securities must be properly safeguarded against loss or destruction. The potential for fraud and loss increases with physically delivered securities.
- Clear delegation of authority to subordinate staff members - Subordinate staff members must have a clear understanding of their authority and responsibilities to avoid improper actions. Clear delegation of authority also preserves the internal control structure that is contingent on the various staff positions and their responsibilities.
- Written confirmation of transactions for investments and wire transfers - Due to the potential for error and improprieties arising from telephone and electronic transactions, all transactions should be supported by written communications and approved by the appropriate person. Written communications may be via fax if on letterhead and if the safekeeping institution has a list of authorized signatures.
- Development of a wire transfer agreement with the lead bank and third-party custodian - The designated official should ensure that an agreement will be entered into and will address the following points: controls, security provisions, and responsibilities of each party making and receiving wire transfers.

Inverted Yield Curve - Chart formation that illustrates long-term securities having lower yields than short-term securities. This configuration usually occurs during periods of high inflation coupled with low levels of confidence in the economy and a restrictive monetary policy.

Investment Company Act of 1940 - Federal legislation which sets the standards by which investment companies, such as mutual funds, are regulated in the areas of advertising, promotion, performance reporting requirements, and securities valuations.

Investment Policy - A concise and clear statement of the objectives and parameters formulated by an investor or investment manager to manage a portfolio of investment securities.

Investment-grade Obligations - An investment instrument suitable for purchase by institutional investors under the prudent person rule. Investment-grade is restricted to those obligations rated BBB or higher by a rating agency.

Liquidity – The ability to convert an asset easily and quickly into cash.

Local Government Investment Pool (LGIP) - An investment by local governments in which their money is pooled as a method for managing local funds.

Mark-to-market - The process whereby the book value or collateral value of a security is adjusted to reflect its current market value.

Market Risk - The risk that the value of a security will raise or decline as a result of changes in market conditions.

Market Value - Current market price of a security.

Maturity - The date on which payment of a financial obligation is due. The final stated maturity is the date on which the issuer must retire a bond and pay the face value to the bondholder. See "Weighted Average Maturity."

Money Market Mutual Funds - Mutual funds that invest solely in money market instruments (short-term debt instruments, such as Treasury bills, commercial paper, bankers' acceptances, repos and federal funds).

Mutual Fund – Pooled money that an investment company invests in a variety of securities, including fixed-income securities and money market instruments. Mutual funds are regulated by the Investment Company Act of 1940 and must abide by the following Securities and Exchange Commission (SEC) disclosure guidelines:

1. Report standardized performance calculations.
2. Disseminate timely and accurate information regarding the fund's holdings, performance, management and general investment policy.
3. Supervise the fund's investment policies and activities by a board of trustees, that is independent of the adviser, administrator, or other vendor of the fund.

4. Maintain the daily liquidity of the fund's shares.
5. Value the funds' portfolios on a daily basis.
6. Allow only individuals who are licensed with a self-regulating organization (SRO) such as National Association of Securities Dealers (NASD) to sell SEC-registered products.
7. Maintain an investment policy governed by a prospectus and update and file with the SEC annually.

Mutual Fund Statistical Services - Companies that track and rate mutual funds, such as IBC/Donoghue, Lipper Analytical Services, and Morningstar.

National Association of Securities Dealers (NASD) - A self-regulatory organization (SRO) of brokers and dealers in the over-the-counter securities business. Its regulatory mandate includes authority over firms that distribute mutual fund shares as well as other securities.

Net Asset Value - The market value of one share of an investment company, such as a mutual fund. This figure is calculated by totaling a fund's assets including securities, cash, and any accrued earnings, subtracting that amount from the fund's liabilities, and then dividing the result by the number of shares outstanding [(Total assets) - (Liabilities)] / (Number of shares outstanding), Net asset value is calculated once a day based on the closing price for each security in the fund's portfolio.

No Load Fund - A mutual fund, which does not levy a sales charge on the purchase of its shares.

Nominal Yield - The stated rate of interest that a bond pays its current owner, based on par value of the security. It is also known as the "coupon," "coupon rate," or "interest rate."

Offer - An indicated price at which market participants are willing to sell a security or commodity, also referred to as the "ask price."

Par - Face value or principal value of a bond, typically \$1,000 per bond.

Positive Yield Curve - A chart formation that illustrates short-term securities having lower yields than long-term securities.

Premium - The amount by which the price paid for a security exceeds the security's par value.

Prime Rate - A preferred interest rate charged by commercial banks to their most creditworthy customers. Many interest rates are keyed to this rate.

Principal - The face value or par value of a debt instrument. Also may refer to the amount of capital invested in a given security.

Prospectus - A legal document that must be provided to any prospective purchaser of a new securities offering registered with the SEC. This can include information on the issuer, the

issuer's business, the proposed use of proceeds, the experience of the issuer's management, and certain certified financial statements.

Prudent Person Rule - An investment standard outlining the fiduciary responsibilities of public funds investors relating to investment practices.

Regular Way Delivery - Securities settlement that calls for delivery and payment on the third business day following the trade date (T+3); payment on a T+1 basis is currently under consideration. Mutual funds are settled on a same day basis; government securities are settled on the next business day.

Reinvestment Risk - The risk that a fixed-income investor will be unable to reinvest income proceeds from a security holding at the same rate of return currently generated by that holding.

Repurchase Agreement (Repo or RP) - An agreement of one party to sell securities at a specified price to a second party and a simultaneous agreement of the first party to repurchase the securities at a specified price or at a specified later date.

Reverse Repurchase Agreement (Reverse Repo) - An agreement of one party to purchase securities at a specified price from a second party and a simultaneous agreement by the first party to resell the securities at a specified price to the second party on demand or at a specified date.

Rule 2a-7 of the Investment Company Act - Applies to all money market mutual funds and mandates such funds to maintain certain standards, including a 13-month maturity limit and a 90-day average maturity on investments, to help maintain a constant net asset value of one dollar (\$1.00).

Safekeeping - Holding of assets (e.g., securities) by a financial institution.

Serial Bond - A bond issue, usually of a municipality, with various maturity dates scheduled at regular intervals until the entire issue is retired.

Sinking Fund - Money accumulated on a regular basis in a separate custodial account that is used to redeem debt securities or preferred stock issues.

Swap - Trading one asset for another.

Term Bond - Bonds comprising a large part or all of a particular issue which come due in a single maturity. The issuer usually agrees to make periodic payments into a sinking fund for mandatory redemption of term bonds before maturity.

Total Return - The sum of all investment income plus changes in the capital value of the portfolio. For mutual funds, return on an investment is composed of share price appreciation plus any realized dividends or capital gains. (Price appreciation) + (Dividends paid) + (Capital gains) = Total Return

Treasury Bills - Short-term U.S. government non-interest bearing debt securities with maturities of no longer than one year and issued in minimum denominations of \$10,000.

Auctions of three and six month bills are held weekly, while auctions of one year bills are held monthly. The yields on these bills are monitored closely in the money markets for signs of interest rate trends.

Treasury Notes - Intermediate U.S. government debt securities with maturities of one to ten years and issued in denominations ranging from \$1,000 to \$1,000,000 or more.

Treasury Bonds - Long term U.S. government debt securities with maturities of ten years or longer and issued in minimum denominations of \$1,000. Currently, the longest outstanding maturity for such securities is 30 years.

Uniform Net Capital Rule - SEC Rule 15C3-1 outlining capital requirements for broker/dealers.

Volatility - A degree of fluctuation in the price and valuation of securities.

"Volatility Risk" Rating - A rating system that indicates the level of volatility and other non-credit risks associated with securities and certain bond funds. The rating for bond funds range from extremely low sensitivity to changing market conditions ("aaa" by S&P; "V-1" by Fitch) to those that are highly sensitive with currently identifiable market volatility risk ("ccc-" by S&P, "V-10" by Fitch).

Weighted Average Maturity (WAM) - The average maturity of all the securities that comprise a portfolio. According to SEC rule 2a-7, the WAM for SEC registered money market mutual funds may not exceed 90 days and no one security may have a maturity that exceeds 397 days.

When Issued (WI) - A conditional transaction in which an authorized new security has not been issued. All "when issued" transactions are settled when the actual security is issued.

Yield - The current rate of return on an investment security generally expressed as a percentage of the security's current price.

Yield-to-call (YTC) - The rate of return an investor earns from a bond assuming the bond is redeemed (called) prior to its nominal maturity date.

Yield-to-maturity - The rate of return yielded by a debt security held to maturity when both interest payments and the investor's potential capital gain or loss are included in the calculation of return.

Zero-coupon Securities - Security that is issued at a discount and makes no periodic interest payments. The rate of return consists of a gradual accretion of the principal of the security and is payable at par upon maturity.

APPENDIX D: RELATED GOVERNMENT CODES

The following references to Government Code are not intended to be a comprehensive statement of the code. To view the full context of the referenced Government Codes please visit www.leginfo.ca.gov and select California Law.

Government Code \ TITLE 2. GOVERNMENT OF THE STATE OF CALIFORNIA \ DIVISION 4. FISCAL AFFAIRS \ PART 2. STATE FUNDS \ CHAPTER 2. SPECIAL FUNDS \ Article 11. Local Agency Investment Fund

GOV §16429.1 There is in trust in the custody of the State Treasurer the Local Agency Investment Fund, which fund is hereby created. Notwithstanding Section 13340, all money in the fund is hereby appropriated without regard to fiscal years to carry out the purpose of this section. The Controller shall maintain a separate account for each governmental unit having deposits in this fund.

Notwithstanding any other provisions of law, a local governmental official, with the consent of the governing body of that agency, having money in its treasury not required for immediate needs, may remit the money to the Treasurer for deposit in the Local Agency Investment Fund for the purpose of investment. The local governmental agency has the exclusive determination of the length of time its money will be on deposit with the Treasurer.

Immediately at the conclusion of each calendar quarter, all interest earned and other increment derived from investments shall be distributed by the Controller to the contributing governmental units in direct proportion to the respective amounts deposited in the Local Agency Investment Fund and the length of time the amounts remained therein. An amount equal to the reasonable costs incurred in carrying out the provisions of this section, not to exceed a maximum of ½ of 1% of the earnings of this fund, shall be deducted from the earnings prior to distribution.

GOV § 16429.4 The right of a city, county, city and county, special district, nonprofit corporation, or qualified quasi-governmental agency to withdrawal its deposited moneys from the Local Agency Investment Fund, upon demand, may not be altered, impaired, or denied, in any way, by and state official or state agency based upon the state's failure to adopt a State Budget by July 1 of each new fiscal year.

Government Code \ TITLE 5. LOCAL AGENCIES \ DIVISION 2. CITIES, COUNTIES, AND OTHER AGENCIES \ PART 1. POWERS AND DUTIES COMMON TO CITIES, COUNTIES, AND OTHER AGENCIES \ CHAPTER 4. FINANCIAL AFFAIRS \ Article 2. Deposit of Funds

GOV § 53601. The legislative body of a local agency having money in a sinking fund of, or

surplus money in, its treasury not required for immediate needs of the local agency may invest any portion of the money that it deems wise or expedient in those investments set forth below. A local agency purchasing or obtaining any securities prescribed in this section, in a negotiable, bearer, registered or non-registered format shall require delivery of the securities to the local agency, including those purchased for the agency by financial advisors, consultants, or managers using the agency's fund, by book entry, physical delivery, or by third party custodial agreement. The transfer of securities to the counterparty bank's customer book entry account may be used for book entry delivery. For purposes of this section "counterparty" means the other party to the transaction. A counterparty bank's trust department or separate safekeeping department may be used for the physical delivery of the security if the security is held in the name of the local agency. Where this section does not specify the limitation on the term or remaining maturity at the time of the investment, no investment may be made in any security other than a security underlying a repurchase or reverse repurchase agreement authorized by this section, that at the time of the investment has a term remaining to maturity in excess of five years, unless the legislative body has granted express authority to make that investment either specifically or as part of an investment program approved by the legislative body no less than three months prior to the investment:

- (a) Bonds issued by the local agency, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the local agency or by a department, board, agency, or authority of the local agency.
- (b) United States Treasury notes, bonds, bills, or certificates of indebtedness, or those for which the faith and credit of the United States are pledged for the payment of principal and interest.
- (c) Registered state warrants or treasury notes or bonds of this state, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the state or by a department, board, agency, or authority of the state.
- (d) Registered treasury notes or bonds of any of the other 49 United States in addition to California, including bonds payable solely out of revenues from revenue-producing property owned, controlled, or operated by a state or a department, board, agency, or authority of any of the other 49 United States, in addition to California.
- (e) Bonds, notes, warrants, or other evidences of indebtedness of any local agency within this state, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the local agency, or by a department, board, agency, or authority of the local agency.
- (f) Federal agency or United States government-sponsored enterprise obligations, participations, or other instruments, including those issued by or fully guaranteed as to principal and interest by federal agencies or United States government-sponsored enterprises.
- (g) Bankers acceptances otherwise known as bills of exchange or time drafts that are drawn on and accepted by a commercial bank. Purchases of bankers acceptances may not exceed 180 days' maturity or 40 percent of the agency's money that may be invested pursuant to this section. However, no more than 30 percent of the agency's money may be invested in the bankers acceptances of any one commercial bank pursuant to this section.

This subdivision does not preclude a municipal utility district from investing any surplus money in its treasury in any manner authorized by the Municipal Utility District Act (Division 6 (commencing with Section 11501) of the Public Utilities Code).

- (h) Commercial paper of "prime" quality of the highest ranking or of the highest letter and numerical rating as provided for by a nationally recognized statistical-rating organization (NRSRO). The entity that issues the commercial paper shall meet all of the following conditions in either paragraph (1) or paragraph (2);
- (1) The entity meets the following criteria:
- (a) Is organized and operating in the United States as a general corporation.
 - (b) Has total assets in excess of five hundred million dollars (\$500,000,000).
 - (c) Has debt other than commercial paper, if any, that is rated "A" or higher by a nationally recognized statistical-rating organization (NRSRO).
- (2) The entity meets the following criteria:
- (a) Is organized within the United States as a special purpose corporation, trust, or limited liability company.
 - (b) Has program wide credit enhancements including, but not limited to, over collateralization, letters of credit, or surety bond.
 - (c) Has commercial paper that is rated "A-1" or higher, or the equivalent, by a Nationally recognized statistical rating organization (NRSRO).

Eligible commercial paper shall have a maximum maturity of 270 days or less. Local agencies, other than a city or county, may invest no more than 25% of their money in eligible commercial paper. Local agencies, other than counties or a city and county, may purchase no more than 10% of the outstanding commercial paper of any single issuer. Counties or a city may invest in commercial paper pursuant to the concentration limits in subdivision (a) of section 53635

- (i) Negotiable certificates of deposit issued by a nationally or state-chartered bank or a state or federal association (as defined by Section 5102 of the Financial Code) or by a state-licensed branch of a foreign bank. Purchases of negotiable certificates of deposit may not exceed 30 percent of the agency's surplus money which may be invested pursuant to this section. For purposes of this section, negotiable certificates of deposit do not come within Article 2 (commencing with Section 53630) except that the amount so invested shall be subject to the limitations of Section 53638. *The legislative body of a local agency and the treasurer or other official of the local agency having legal custody of the money are prohibited from investing local agency funds, or funds in the custody of the local agency, in negotiable certificates of deposit issued by a state or federal credit union if a member of the legislative body of the local agency, or any person with investment decision making authority in the administrative office manager's office, budget office, or treasurers office of the local agency also serves on the board of directors, or any committee appointed by the board of directors, or the credit committee or the supervisory committee of the state or federal credit union issuing the negotiable certificates of deposit.*
- (j) (1) Investments in repurchase agreements or reverse repurchase agreements of any securities authorized by this section, as long as the agreements are subject to this

subdivision, including the delivery requirements specified in this section.

- (2) Investments in repurchase agreements may be made, on any investment authorized in this section, when the term of the agreement does not exceed one year. The market value of securities that underlay a repurchased agreement shall be valued at 102 percent or greater of the funds borrowed against those securities and the value shall be adjusted no less than quarterly.
 - (3) *Omitted*: Pertains to reverse repurchase agreements, as the City does not allow this type of investment it is not pertinent to us.
 - (4) *Omitted*: Pertains to reverse repurchase agreements, as the City does not allow this type of investment it is not pertinent to us.
 - (5) (A) "Repurchase agreement" means a purchase of securities by the local agency pursuant to an agreement by which the counterparty seller will repurchase the securities on or before a specified date and for a specified amount and the counterparty will deliver the underlying securities to the local agency by book entry, physical delivery, or by third party custodial agreement. The transfer of underlying securities to the counterparty bank's customer book-entry account may be used for book-entry delivery.

(B) "Securities," for purpose of repurchase under this subdivision, means securities of the same issuer, description, issue date, and maturity.
- (k) Medium-term notes, defined as all corporate and depository institution debt securities with a of a maximum remaining maturity of five years or less, issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States. Notes eligible for investment under this subdivision shall be rated in a rating category of "A" or its equivalent or better by a nationally recognized rating service. Purchases of medium-term notes shall note include other instruments authorized by this section and may not exceed 30 percent of the agency's surplus money which may be invested pursuant to this section.
- (l) (1) Shares of beneficial interest issued by diversified management companies that invest in the securities and obligations as authorized by subdivisions (a) to (j), inclusive, or subdivision (m) or (n) and that comply with the investment restrictions of this article and Article 2 (commencing with Section 53630). However, notwithstanding these restrictions, a counterparty to a reverse repurchase agreement is not required to be a primary dealer of the Federal Reserve Bank of New York if the company's board of directors finds that the counterparty presents a minimal risk of default, and the value of the securities underlying a repurchase agreement may be 100 percent of the sales price if the securities are marked to market daily.
- (2) Shares of beneficial interest issued by diversified management companies 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.).
 - (3) If investment is in shares issued pursuant to paragraph (1), the company shall have met either of the following criteria:

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- (A) Attained the highest ranking or the highest letter and numerical rating provided by not less than two nationally recognized statistical rating organizations.
 - (B) Retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience investing in the securities and obligations authorized by subdivisions (a) to (j), inclusive, or subdivision (m) or (n) and with assets under management in excess of five hundred million dollars (\$500,000,000).
- (4) If investment is in shares issued pursuant to paragraph (2), the company shall have met either of the following criteria:
- (A) Attained the highest ranking or the highest letter and numerical rating provided by not less than two nationally recognized statistical rating organizations.
 - (B) Retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience managing money market mutual funds with assets under management in excess of five hundred million dollars (\$500,000,000).
- (5) The purchase price of shares of beneficial interest purchased pursuant to this subdivision shall not include any commission that the companies may charge and shall not exceed 20 percent of the agency's money that may be invested pursuant to this section. However, no more than 10 percent of the agency's surplus funds may be invested in shares of beneficial interest of any one mutual fund pursuant to paragraph (1).
- (m) Moneys held by trustee or fiscal agent and pledged to the payment or security of bonds or other indebtedness, or obligations under a lease, installment sale, or other agreement of a local agency, or certificates of participation in those bonds, indebtedness, or lease installment sale, or other agreements, may be invested in accordance with the statutory provisions governing the issuance of those bonds, indebtedness or lease installment sale, or other agreement, or to the extent not inconsistent therewith or if there are no specific statutory provisions, in accordance with the ordinance, resolution, indenture, or agreement of the local agency providing for the issuance.
- (n) Notes, bonds, or other obligations that are at all times secured by a valid first priority security interest in securities of the types listed by Section 53651 as eligible securities for the purpose of securing local agency deposits having a market value at least equal to that required by Section 53652 for the purpose of securing local agency deposits. The securities serving as collateral shall be placed by delivery or book entry into the custody of a trust company or the trust department of a bank which is not affiliated with the issuer of the secured obligation, and the security interest shall be perfected in accordance with the requirements of the Uniform Commercial Code or federal regulations applicable to the types of securities in which the security interest is granted.
- (o) Any mortgage pass-through security, collateralized mortgage obligation, mortgage-backed or other pay-through bond, equipment lease-backed certificate, consumer
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receivable pass-through certificate, or consumer receivable-backed bond of a maximum of five years maturity. Securities eligible for investment under this subdivision shall be issued by an issuer having an "A" or higher rating for the issuer's debt as provided by a nationally recognized rating service and rated in a rating category of "AA" or its equivalent or better by a nationally recognized rating service. Purchase of securities authorized by this subdivision may not exceed 20 percent of the agency's surplus money that may be invested pursuant to this section. [As affected by 1996 legislation]

- (p) Shares of beneficial interest issued by a joint powers authority organized pursuant to Section 6509.7 that invests in the securities and obligations authorized in subdivisions (a) to (o), inclusive. Each share shall represent an equal proportional interest in the underlying pool of securities owned by the joint powers authority. To be eligible under this section, the joint powers authority issuing the shares shall have retained an investment advisor that meets all of the following criteria:
- (1) The advisor is registered or exempt from registration with the Securities and Exchange Commission.
 - (2) The advisor has not less than five years of experience investing in the securities and obligations authorized in subdivisions (a) to (o), inclusive.
 - (3) The advisor has assets under management in excess of five hundred million dollars (\$500,000,000).

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GOV § 53601.6. (a) A local agency shall not invest any funds pursuant to this article or pursuant to Article 2 (commencing with section 53630) in inverse floaters, range notes, or mortgage-derived, interest only strips.

(b) A local agency shall not invest any funds pursuant to this article or pursuant to Article 2 (commencing with Section 53630) in any security that could result in zero interest accrual if held to maturity. However, a local agency may hold prohibited instruments until their maturity dates. The limitation in this subdivision shall not apply to local agency investments in shares of beneficial interest issued by diversified management companies registered under the Investment Company Act of 1940 (15 U.S. SEC. 80a-1, and following) that are authorized for investment pursuant to subdivision (k) of Section 53601.[As affected by 1995 legislation]