

City of Banning Administrative Policy

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| Subject: | Statement of Investment Policy | Policy No: |
| Reference: | Financial Management, Accounting and Purchasing | Effective: June 13, 2023 |
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1. SCOPE

This Statement of Investment Policy pertains to those funds under the control of the City Council, designated for the ongoing operations of the City, the Banning Finance Authority, the Banning Utility Authority and the Successor Agency to the City of Banning Redevelopment Agency. The Statement of Investment Policy concerns the deposit, maintenance, and safekeeping of all such funds, and the investments made with these funds. This Policy does not apply to pension funds, deferred compensation funds, bond funds (the investment of which is governed by the bond documents), trustee, and certain other non-operating funds.

The City Council must ensure management of public monies in a way that is consistent with investment oversight and sound investment practices. To have a policy which only concerns itself with maximizing return is reckless. The basic concept of investment management is the risk/reward relationship. A higher promised return on any investment may indicate a higher level of risk. Risk management must be an integral part of any prudent investment policy. Risk management must include adequate internal controls, so the public has confidence that public monies are secure. Though all investments contain a degree of risk, the proper exercise of prudence, the maintenance of a high level of ethical standards, and the proper delegation of authority reduces the potential for loss.

The Administrative Services Director may direct specific-purpose assets belonging to the City, the earnings of which are not shared but credited to the specific-purpose fund. The investments for these direct investment pools shall be made in accordance with this Policy, except that investments may be for periods greater than five years when a longer term is advantageous for the investment of money held for specific purposes. Investments for periods longer than five years require prior approval of the governing body in accordance with Government Code Section 53601.

2. PURPOSE OF POLICY STATEMENT

The purpose of this Statement of Investment Policy is to provide the public and those involved in servicing the investment requirements of the City, and any other interested party, a clearer understanding of the Government Code, regulations and internal guidelines that will be observed in maintaining and investing those funds not immediately needed to meet liabilities. This policy is written to incorporate industry best practices and recommendations from sources such as the Government Finance Officers Association (GFOA), California Municipal Treasurers Association

(CMTA), California Debt and Investment Advisory Commission (CDIAC) and the Association of Public Treasurers (APT).

3. INVESTMENT OBJECTIVES

The underlying objective of the City Council is to protect the safety of the principal of the portfolio through the judicious purchase of those legal investments permitted to local agencies, as defined in the State of California Government Code, consistent with current conditions and the other dominant objectives pursuant to managing a local agency portfolio. The objectives of this Investment Policy are, in order of priority:

- A. Safety. The City Council takes as its primary responsibility to maintain the safe return of all principal placed in investments by avoiding decisions that might result in losses through fraud, default, or adverse market conditions. Importance is also accorded to the protection of accrued interest earned on any investment instrument. To attain this objective, the City will diversify its investments by investing funds among a variety of securities with independent returns.
- B. Liquidity. The investment portfolio will remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated.
- C. Yield. While it is considered desirable to obtain a respectable yield, yield shall not be the driving force in determining which investments are to be selected for purchase. Yield is to be given lesser weight in the investment decision than safety, liquidity, or availability. Investment shall be placed with the objective of obtaining a reasonable rate of return under prevailing market conditions.

4. PRUDENCE

The City Council and the City's investment officials recognize that they are subject to the "Prudent Investor Standard" whenever making a decision regarding the investment of the City's funds. The Prudent Investor Standard states, "...all governing bodies of local agencies or persons authorized to make investment decisions on behalf of those local agencies investing public funds pursuant to this chapter are trustees and therefore fiduciaries subject to the prudent investor standard. When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, general economic conditions and the anticipated needs of the agency, that a prudent person acting in like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency. Within the limitations of this section and considering individual investments as part of an overall strategy, investments may be acquired as authorized by law." (Cal. Gov. Code §53600.3).

The City Council, and those acting under the delegation of authority of the City Council, are deemed to have a fiduciary trustee relationship with the public for the public funds, and all investment decisions will be made in accordance with their fiduciary duties.

5. DELEGATION OF AUTHORITY

Authority to manage the City's investment program is derived from California Government Code, Sections 41006 and 53600 *et seq.*

While the City Council has fiduciary responsibility for the investment of public funds, City personnel are required to act in the day to day administration of the City's investment program.

The deputized personnel (also referred to as investment officials) listed below are designated to manage the City's investment program consistent with this investment policy:

- Administrative Services Director
- Deputy Finance Director
- City Manager

City Council directives to the Administrative Services Director, Deputy Finance Director and City Manager are as follows:

- Manage the day to day operations of the City's investment portfolio and place actual purchase/sell orders with authorized institutions.
- Make investments in accordance with this policy.
- Communicate with necessary parties for investment purposes and to withdraw and deposit funds as required to meet the City's cash flow needs.

Other persons, both inside and outside City employment, may act in the role of assistant or advisor to those listed above, to aid in the timely and proper settlement of investment transactions. Such persons may not authorize, approve, or initiate any trading activities. Parties involved in investment transactions with the City are deemed to be on notice of the contents of the most current copy of this Policy, and all pertinent authorizing documents, at the time of accepting written or verbal instructions from any staff member.

The City may engage the services of one or more external investment advisers, who are registered under the Investment Advisers Act of 1940, to assist in the management of the City's investment portfolio in a manner consistent with the City's objectives. External investment advisers may be granted discretion to purchase and sell investment securities in accordance with this investment policy.

The City's overall investment program shall be designed and managed with a degree of professionalism that is worthy of the public trust. The City recognizes that in a diversified portfolio, occasional measured losses may be inevitable and must be considered within the context of the overall portfolio's return and the cash flow requirements of the City.

6. SECURITIES CUSTODY

As required by the Government Code, the Administrative Services Director shall establish a third party custody and safekeeping account to which all negotiable instruments shall be delivered upon purchase on a payment versus delivery basis. All cash and securities in the City's portfolio

shall be held in safekeeping in the City's name by the third party custodian, acting as an agent for the City under the terms of a custody agreement executed by the bank and the City.

The only exceptions to the foregoing shall be depository accounts and securities purchases made with: (i) local government investment pools; (ii) time certificates of deposit, and, (iii) mutual funds and money market mutual funds, since these securities are not deliverable.

7. AUTHORIZED INVESTMENTS AND LIMITATIONS

The Government Code of the State of California, primarily within sections 53600 et. seq., sets out the legal authority for inclusion of certain types of investment vehicles in a California local agency's investment portfolio. Consistent with those sections, under no circumstances will the City Council purchase an investment that is not specifically authorized for a local agency under these, or other code sections that may apply, or might later be enacted, pertaining to local agency investments. It shall be a requirement of all investment professionals performing any transaction on behalf of the City that they possess a complete understanding of the acceptability of the subject investment under those code sections.

Appendix A briefly describes the principal types of securities legal within the Government Code sections noted above, and outlines the various limitations included in these sections. From these permitted investments, the City's investment officials shall determine those investment types that best meet the needs and abilities of the City.

Any investment currently held at the time the policy is adopted which does not meet the new policy guidelines can be held until maturity and shall be exempt from the current policy. At the time of the investment's maturity or liquidation, such funds shall be reinvested only as provided in the current policy.

An appropriate risk level shall be maintained by primarily purchasing securities that are of high quality, liquid, and marketable. The portfolio shall be diversified by security type and institution to avoid incurring unreasonable and avoidable risks regarding specific security types or individual issuers.

A. Prohibited Investment Vehicles and Practices

- State law notwithstanding, any investments not specifically described herein are prohibited, including, but not limited to futures and options.
- In accordance with Government Code, Section 53601.6, investment in inverse floaters, range notes, or mortgage derived interest-only strips is prohibited.
- Investment in any security that could result in a zero interest accrual if held to maturity is prohibited. Under a provision sunsetting on January 1, 2026, securities backed by the U.S. Government that could result in a zero- or negative-interest accrual if held to maturity are permitted.
- Trading securities for the sole purpose of speculating on the future direction of interest rates is prohibited.
- Purchasing or selling securities on margin is prohibited.

- The use of reverse repurchase agreements, securities lending or any other form of borrowing or leverage is prohibited.
- The purchase of foreign currency denominated securities is prohibited.
- Agencies that are not Qualified Institutional Buyers (QIB) as defined by the Securities and Exchange Commission are prohibited from purchasing Private Placement Securities. The SEC defines a QIB as having at least \$100,000,000 in securities owned and invested.
- The purchase of a security with a forward settlement date exceeding 45 days from the time of the investment is prohibited.

8. AUTHORIZED TERM OF INVESTMENTS

It is hereby determined that the maximum maturity period for any portion of invested operating moneys shall not exceed five years from the date of trade settlement per California Government Code and as indicated in Appendix A, unless the City Council has by resolution granted authority to make such an investment. This shall not apply to certain bond proceeds or other non-operating moneys of the City. To the extent possible, investments shall be matched with anticipated cash flow requirements and known future liabilities.

9. AUTHORIZED DEALER LIST - CONFLICT OF INTEREST PROHIBITION

It is prohibited for a transaction to be entered into with any securities broker, dealer or bank investment department or subsidiary prior to that entity being designated an Authorized Dealer and placed on the Authorized Dealer List. Authorized Dealers shall be selected on an as needed basis to meet specific needs of the City. The Administrative Services Director is authorized to manage the Authorized Dealer List. Each qualified dealer must certify in writing that they have reviewed the relevant California Government Code Sections and the City's Investment Policy and that all securities offered to the City shall comply fully and in every instance with all provisions of the California Government Code and with this Investment Policy. Selection of financial institutions and broker/dealers authorized to engage in transactions will be at the sole discretion of the City, except where the City utilizes an external investment adviser in which case the Agency may rely on the adviser for selection.

In accordance with Section 53601.5, institutions eligible to transact investment business with the City include:

- Institutions licensed by the state as a broker-dealer.
- Institutions that are members of a federally regulated securities exchange.
- Primary government dealers as designated by the Federal Reserve Bank and non-primary government dealers.
- Nationally or state-chartered banks.
- The Federal Reserve Bank.
- Direct issuers of securities eligible for purchase.

Selection of broker/dealers used by an external investment adviser retained by the City will be at the sole discretion of the adviser. Where possible, transactions with broker/dealers shall be selected on a competitive basis and their bid or offering prices shall be recorded. If there is no other readily available competitive offering, best efforts will be made to document quotations for comparable or

alternative securities. When purchasing original issue instrumentality securities, no competitive offerings will be required as all dealers in the selling group offer those securities at the same original issue price.

No member of the City Council, nor any other official or employee of the City, may accept any gift, honoraria, gratuity or service of value in violation of the regulations set forth by the Fair Political Practices Commission, the Government Code, additional limitations set forth by City ordinance, or internal requirements of the City Manager and Administrative Services Director. The City Council is prohibited from conducting any business with any broker, dealer, or securities firm that has made a political contribution to the City Treasurer or any member of the City Council, or any candidate for these offices, within the 48 month period immediately following the date of the political contribution, in an amount exceeding the limitation contained in Rule G-37 of the Municipal Securities Rulemaking Board.

10. PORTFOLIO RISK MANAGEMENT

A. Mitigating Credit Risk in the Portfolio

Credit risk is the risk that a security or a portfolio will lose some or all of its value due to a real or perceived change in the ability of the issuer to repay its debt. The Administrative Services Director shall mitigate credit risk by adopting the following strategies:

1. The diversification requirements included in Appendix A Permitted Investments are designed to mitigate credit risk in the portfolio.
2. The City may elect to sell a security prior to its maturity and record a capital gain or loss in order to improve the quality, liquidity or yield of the portfolio in response to market conditions or the City's risk preferences.
3. No more than 5% of the total portfolio may be deposited with or invested in securities issued by any single issuer unless otherwise specified in this policy.
4. If the securities owned by the City are downgraded by Moody's, S&P, or Fitch to a level below the quality required by this Investment Policy, it shall be the City's policy to review the credit situation and make a determination as to whether to sell or retain such securities in the portfolio. City investment officials will use discretion in determining whether to sell or hold the security based on its current maturity, the loss in value, the economic outlook for the issuer, and other relevant factors.
5. The City will continue to monitor and reevaluate the security on an ongoing basis in order to reaffirm or change the decision to hold a downgraded security.
6. If a decision is made to retain a downgraded security in the portfolio, the status of the investment will be reported quarterly to the City Council.

B. Mitigating Market Risk in the Portfolio

Market risk is the risk that the portfolio will decline in value (or will not optimize its value) due to changes in the general level of interest rates. The City recognizes that, over time, longer-term portfolios generally achieve higher returns. On the other hand, longer-term portfolios have a higher volatility of return. The City shall mitigate market risk by providing adequate liquidity for cash needs, and by making longer-term investments only with funds that are not needed for current cash flow purposes. The City further recognizes that certain types of securities, including variable rate securities, and securities with embedded options, will affect the market risk profile of the portfolio differently in different interest rate environments. The City, therefore, adopts the following strategies to control and mitigate its exposure to market risk:

1. All investments are categorized according to the period of time from settlement date to maturity date. Market circumstances and risk-return calculations for increased yield may require an extended schedule.
2. The maximum stated final maturity of individual securities in the portfolio shall be five years, except as otherwise stated in this policy. The five-year maturity of callable securities is measured to the final maturity date, not to a call date.
3. Maturity of investments should be governed by the Treasury's demand for funds through analysis of revenue and expenditure activity over prior periods. The portfolio shall be structured in such manner that securities mature concurrent with cash needs.
4. The duration of the portfolio will generally be approximately equal to the duration (typically, plus or minus 20%) of a market benchmark, and index selected by the City based on the City's investment objectives, constraints and risk tolerances.

C. Mitigating Reinvestment Risk in the Portfolio

Reinvestment risk is the risk that cash flows from securities will be reinvested at interest rates that are lower than the rate of the original investment. Securities that are highly subject to reinvestment risk include mortgage-backed and callable securities. The City, therefore, adopts the following strategies to control and mitigate its exposure to reinvestment risk:

1. The portfolio shall include securities with a range of durations and maturities.
2. Investment in federal agency callable securities is limited to 20%.

11. LEGISLATIVE CHANGES

Any State of California legislative action that further restricts allowable maturities, investment type, or percentage allocations will be incorporated immediately into the Investment Policy.

12. REPORTING AND ANNUAL REVIEW

The Administrative Services Director shall cause to be maintained investment records legally required or otherwise requested by the City Council and prepare a report for the Council on a

monthly basis stating the holdings, status, and earnings of the portfolio. The Statement of Investment Policy will be provided annually for review and approval of the City Council. Should conditions arise, or legislation become effective that behooves consequential changes within the Policy during the year, the revised policy will again be addressed by the City Council.

APPENDIX A **PERMITTED INVESTMENTS**

- 1. Municipal Securities** include obligations of the City, the State of California and any local agency within the State of California, provided that:
 - The securities are rated in a rating category of “A” or its equivalent or better by at least one nationally recognized statistical rating organization (“NRSRO”).
 - No more than 5% of the portfolio may be invested in any single issuer.
 - No more than 30% of the portfolio may be in Municipal Securities.
 - The maximum maturity does not exceed five (5) years.
- 2. MUNICIPAL SECURITIES (REGISTERED TREASURY NOTES OR BONDS)** of any of the other 49 states in addition to California, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of any of the other 49 states, in addition to California.
 - The securities are rated in a rating category of “A” or its equivalent or better by at least one nationally recognized statistical rating organization (“NRSRO”).
 - No more than 5% of the portfolio may be invested in any single issuer.
 - No more than 30% of the portfolio may be in Municipal Securities.
 - The maximum maturity does not exceed five (5) years.
- 3. U.S. TREASURIES** and other government obligations for which the full faith and credit of the United States are pledged for the payment of principal and interest. There are no limits on the dollar amount or percentage that the City may invest in U.S. Treasuries, provided that:
 - The maximum maturity is five (5) years.
- 4. FEDERAL AGENCIES** 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. There are no limits on the dollar amount or percentage that the City may invest in Federal Agency or Government-Sponsored Enterprises (GSEs), provided that:
 - No more than 30% of the portfolio may be invested in any single Agency/GSE issuer.
 - The maximum maturity does not exceed five (5) years.
 - The maximum percent of agency callable securities in the portfolio will be 20%.
- 5. BANKER’S ACCEPTANCES**, provided that:
 - They are issued by institutions which have short-term debt obligations rated “A-1” or its equivalent or better by at least one NRSRO; or long-term debt obligations which are rated in a rating category of “A” or its equivalent or better by at least one NRSRO.
 - No more than 40% of the portfolio may be invested in Banker’s Acceptances.
 - No more than 5% of the portfolio may be invested in any single issuer.

- The maximum maturity does not exceed 180 days.

6. COMMERCIAL PAPER, provided that the securities are issued by an entity that meets all of the following conditions in either paragraph (a) or (b) and other requirements specified below:

- a. **SECURITIES** issued by corporations:
 - (i) A corporation organized and operating in the United States with assets more than \$500 million.
 - (ii) The securities are rated “A-1” or its equivalent or better by at least one NRSRO.
 - (iii) If the issuer has other debt obligations, they must be rated in a rating category of “A” or its equivalent or better by at least one NRSRO.
- b. **SECURITIES** issued by other entities:
 - (i) The issuer is organized within the United States as a special purpose corporation, trust, or limited liability company.
 - (ii) The securities must have program-wide credit enhancements including, but not limited to, overcollateralization, letters of credit, or a surety bond.
 - (iii) The securities are rated “A-1” or its equivalent or better by at least one NRSRO.

- No more than 10% of the outstanding commercial paper of any single issuer.
- No more than 25% of the City’s investment assets under management may be invested in Commercial Paper. Under a provision sunsetting on January 1, 2026, no more than 40% of the portfolio may be invested in Commercial Paper if the Agency’s investment assets under management are greater than \$100,000,000.
- No more than 5% of the portfolio may be invested in any single issuer.
- The maximum maturity does not exceed 270 days.

7. NEGOTIABLE CERTIFICATES OF DEPOSIT (NCDs), issued by a nationally or state-chartered bank, a savings association or a federal association, a state or federal credit union, or by a federally licensed or state-licensed branch of a foreign bank, provided that:

- The amount of the NCD insured up to the FDIC limit does not require any credit ratings.
- Any amount above the FDIC insured limit must be issued by institutions which have short-term debt obligations rated “A-1” or its equivalent or better by at least one NRSRO; or long-term obligations rated in a rating category of “A” or its equivalent or better by at least one NRSRO.
- No more than 30% of the total portfolio may be invested in NCDs (combined with CDARS).
- No more than 5% of the portfolio may be invested in any single issuer.
- The maximum maturity does not exceed five (5) years.

8. FEDERALLY INSURED TIME DEPOSITS (Non-Negotiable Certificates of Deposit) in state or federally chartered banks, savings and loans, or credit unions, provided that:

- The amount per institution is limited to the maximum covered under federal insurance.

- No more than 20% of the portfolio will be invested in a combination of federally insured and collateralized time deposits.
- The maximum maturity does not exceed five (5) years.

9. COLLATERALIZED TIME DEPOSITS (Non-Negotiable Certificates of Deposit) in state or federally chartered banks, savings and loans, or credit unions in excess of insured amounts which are fully collateralized with securities in accordance with California law, provided that:

- No more than 20% of the portfolio will be invested in a combination of federally insured and collateralized time deposits.
- The maximum maturity does not exceed five (5) years.

10. CERTIFICATE OF DEPOSIT PLACEMENT SERVICE (CDARS), provided that:

- No more than 30% of the total portfolio may be invested in a combination of Certificates of Deposit, including CDARS.
- The maximum maturity does not exceed five (5) years.

11. COLLATERALIZED BANK DEPOSITS. City's deposits with financial institutions will be collateralized with pledged securities per California Government Code, Section 53651. There are no limits on the dollar amount or percentage that the City may invest in collateralized bank deposits.

12. REPURCHASE AGREEMENTS collateralized with securities authorized under California Government Code, maintained at a level of at least 102% of the market value of the Repurchase Agreement. There are no limits on the dollar amount or percentage that the City may invest, provided that:

- Securities used as collateral for Repurchase Agreements will be delivered to an acceptable third party custodian.
- Repurchase Agreements are subject to a Master Repurchase Agreement between the City and the provider of the repurchase agreement. The Master Repurchase Agreement will be substantially in the form developed by the Securities Industry and Financial Markets Association (SIFMA).
- The maximum maturity does not exceed one (1) year.

13. STATE OF CALIFORNIA LOCAL AGENCY INVESTMENT FUND (LAIF), provided that:

- The City may invest up to the maximum amount permitted by LAIF.
- LAIF's investments in instruments prohibited by or not specified in the City's policy do not exclude the investment in LAIF itself from the City's list of allowable investments, provided LAIF's reports allow the Administrative Services Director to adequately judge the risk inherent in LAIF's portfolio.

14. LOCAL GOVERNMENT INVESTMENT POOLS

- Other LGIPs permitted by client.

- There is no issuer limitation for Local Government Investment Pools

15. CORPORATE MEDIUM TERM NOTES (MTNs), provided that:

- The issuer is a corporation 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.
- The securities are rated in a rating category of “A” or its equivalent or better by at least one NRSRO.
- No more than 30% of the total portfolio may be invested in MTNs.
- No more than 5% of the portfolio may be invested in any single issuer.
- The maximum maturity does not exceed five (5) years.

16. ASSET-BACKED, MORTGAGE-BACKED, MORTGAGE PASS-THROUGH SECURITIES, AND COLLATERALIZED MORTGAGE OBLIGATIONS FROM ISSUERS NOT DEFINED IN SECTIONS 3 AND 4 OF THE AUTHORIZED INVESTMENTS SECTION OF THIS POLICY, provided that:

- The securities are rated in a rating category of “AA” or its equivalent or better by a NRSRO.
- No more than 20% of the total portfolio may be invested in these securities.
- No more than 5% of the portfolio may be invested in any single Asset-Backed or Commercial Mortgage security issuer.
- The maximum legal final maturity does not exceed five (5) years.

17. MUTUAL FUNDS AND MONEY MARKET MUTUAL FUNDS that are registered with the Securities and Exchange Commission under the Investment Company Act of 1940, provided that:

- a. **MUTUAL FUNDS** that invest in the securities and obligations as authorized under California Government Code, Section 53601 (a) to (k) and (m) to (q) inclusive and that meet either of the following criteria:
 - (i) Attained the highest ranking or the highest letter and numerical rating provided by not less than two (2) NRSROs; or
 - (ii) Have 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 California Government Code, Section 53601 and with assets under management in excess of \$500 million.
- No more than 10% of the total portfolio may be invested in shares of any one mutual fund.
- b. **MONEY MARKET MUTUAL FUNDS** registered with the Securities and Exchange Commission under the Investment Company Act of 1940 and issued by diversified management companies and meet either of the following criteria:
 - (i) Have attained the highest ranking or the highest letter and numerical rating provided by not less than two (2) NRSROs; or

- (ii) Have 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 \$500 million.
- No more than 20% of the total portfolio may be invested in the shares of any one Money Market Mutual Fund.
- c. No more than 20% of the total portfolio may be invested in these securities.

18. SUPRANATIONALS, provided that:

- Issues are US dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank.
- The securities are rated in a rating category of "AA" or its equivalent or better by a NRSRO.
- No more than 30% of the total portfolio may be invested in these securities.
- No more than 10% of the portfolio may be invested in any single issuer.
- The maximum maturity does not exceed five (5) years.

APPENDIX B GLOSSARY OF TERMS

ACCRUED INTEREST – The amount of interest that is earned, but unpaid since the last payment date.

BANKERS ACCEPTANCES – A draft or bill or exchange accepted by a bank or trust company. The accepting institution, as well as the issuer, guarantees payment of the bill. With the credit strength of a bank behind it, the bankers acceptance usually qualifies as a money market instrument. In its simplest and most traditional form, a bankers acceptance is merely a check drawn on a bank by an importer or exporter of goods.

BASIS POINT - A unit of measurement used in the valuation of fixed-income securities equal to 1/100 of 1 percent of yield, e.g., "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 ENTRY – The system maintained by the Federal Reserve, by which most money market securities are delivered to an investor's custodian bank. The Federal Reserve maintains a computerized record of the ownership of these securities and records any changes in ownership corresponding to payments made over the Federal Reserve wire (delivery versus payment).

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.

BROKER/DEALER – Any person engaged in the business of effecting transactions in securities in this state for the account of others or for her/his own account. Broker/dealer also includes a person engaged in the regular business of issuing or guaranteeing options with regard to securities not of her/his own issue.

CALIFORNIA DEBT AND INVESTMENT ADVISORY COMMISSION (CDIAC)- The CDIAC provides information, education, and technical assistance on public debt and investments to local public agencies and other public finance professionals.

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 including:

CERTIFICATES OF DEPOSIT (CDS) - The City shall require any commercial bank or savings and loan association to deposit eligible securities with an agency of a depository approved by the State Banking Department to secure any uninsured portion of a Non-Negotiable Certificate of Deposit. The value of eligible securities as defined pursuant to California Government Code, Section 53651, pledged against a Certificate of Deposit shall be equal to 150% of the face value of the CD if the securities are classified as mortgages and 110% of the face value of the CD for all other classes of security.

COLLATERALIZATION OF BANK DEPOSITS - This is the process by which a bank or financial institution pledges securities, or other deposits for the purpose of securing repayment of deposited funds. The City shall require any bank or financial institution to comply with the collateralization criteria defined in California Government Code, Section 53651.

REPURCHASE AGREEMENTS - The City requires that Repurchase Agreements be collateralized only by securities authorized in accordance with California Government Code:

- The securities which collateralize the repurchase agreement shall be priced at Market Value, including any Accrued Interest plus a margin. The Market Value of the securities that underlie a repurchase agreement shall be valued at 102% or greater of the funds borrowed against those securities.
- Financial institutions shall mark the value of the collateral to market at least monthly and increase or decrease the collateral to satisfy the ratio requirement described above.
- The City shall receive monthly statements of collateral.

COMMERCIAL PAPER - An unsecured short-term promissory note issued by banks, corporations and other borrowers with temporarily idle cash, with maturities ranging from 2 to 270 days. Such instruments are usually discounted, although some are interest bearing. It is issued only by top-rated concerns and is nearly always backed by bank lines of credit.

CONFIRMATION – Formal memorandum from a broker/dealer to the City giving the details of a securities transaction, i.e., purchase or sale.

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.

CUSTODIAN/CUSTODY – The financial institution where the investments purchased by the City are held.

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 - 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 – The spreading of risk by investing in 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.

EARNINGS APPORTIONMENT – The quarterly interest distribution to the Investment Pool participants where the actual investment costs incurred by the City are deducted from the interest earnings of the Investment Pool.

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 - 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.

FITCH IBCA, INC. (FITCH) – One of the three best known rating agencies in the United States, the others being Moody's Investment Service, Inc. (Moody's), and Standard and Poor's Corporation (S & P).

GUARANTEED INVESTMENT CONTRACTS (GICS) – An agreement acknowledging receipt of funds for deposit, specifying terms for withdrawal, and guaranteeing a rate of interest to be paid.

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."

HIGHLY LIQUID – The most eminent type of security that is easily converted to cash because there are many interested buyers and sellers to trade large quantities at a reasonable price.

IDLE FUNDS – funds in the combined Investment Pool not required for immediate cash needs.

ILLIQUID – A security that is difficult to buy or sell or has a wide spread between bid price and offer price in the secondary market. There are few buyers and sellers willing to trade large quantities at a reasonable price.

INFORMAL COMPETITIVE BID – A verbal or written bid submitted to the City by a broker/dealer for a specific issue at a specific price or yield.

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 - An internal control structure designed to ensure that the assets of the entity are protected from loss, theft, or misuse. The internal control structure is designed to provide reasonable assurance that these objectives are met. 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:

1. Control of collusion - Collusion is a situation where two or more employees are working in conjunction to defraud their employer.
2. 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.
3. 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.
4. 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.
5. 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 respective responsibilities.
6. 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.
7. 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 - A 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 POLICY - A concise and clear statement of the objectives and parameters formulated by an investor or investment manager for 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.

LIQUID - An asset that can be converted easily and quickly into cash because of the willingness of interested buyers and sellers to trade large quantities at a reasonable price.

LOCAL AGENCY INVESTMENT FUND (LAIF) - The State of California investment pool in which money of local agencies is pooled as a method for managing and investing local funds.

LOCAL AGENCY OBLIGATION - An indebtedness issued by a local agency, department, board, or authority within the State of California.

LONG-TERM - A security with the maturity greater than one year.

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 rise or decline as a result of changes in market conditions.

MARKET VALUE - The price at which a security is trading and presumably could be purchased or sold at a particular point in time.

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."

MEDIUM TERM NOTES - Corporate Notes and Deposit Notes that are obligations of banks, corporations, and insurance companies. They are issued at a specific rate of return for a specific period of time.

MONEY MARKET MUTUAL FUND - 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).

MOODY'S INVESTORS SERVICE, INC. (Moody's) - One of the three best known rating

agencies in the United States, the others being Standard and Poor's Corporation (S& P) and Fitch IBCA, Inc. (Fitch).

MUTUAL FUND - An investment company that pools money and can invest 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. Have the fund's investment policies and activities supervised by a board of trustees, which are independent of the adviser, administrator or other vendor of the fund.
4. Maintain the daily liquidity of the fund's shares.
5. Value their portfolios on a daily basis.
6. Have all individuals who sell SEC-registered products licensed with a self-regulating organization (SRO) such as the National Association of Securities Dealers (NASD).
7. Have an investment policy governed by a prospectus which is updated and filed by the SEC annually.

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.

NEGOTIABLE CERTIFICATE OF DEPOSIT – A Money Market instrument representing a receipt from a bank for a deposit at a specified rate of interest for a specified period of time that is traded in the secondary markets.

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 which includes securities, cash, and any accrued earnings, subtracting this from the fund's liabilities and dividing this total by the number of shares outstanding. This 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."

NONCALLABLE – A bond that is exempt from any kind of redemption for a stated time period.

NOTE – A written promise to pay a specific amount to a certain entity on demand or on a specified date.

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.

PORTFOLIO – Combined holding of more than one stock, bond, cash equivalent, or other asset. The purpose of a portfolio is to reduce risk by diversification.

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.

PRIMARY DEALER – A group of securities dealers that submit daily reports of market activity and positions and monthly financial statements to the Federal Reserve Bank of New York and are subject to its informal oversight. Primary dealers include Securities and Exchange Commission (SEC) registered securities broker-dealers and banks.

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 (also known as an "official statement").

PRUDENT INVESTOR RULE - An investment standard where a person acts with care, skill, prudence, and diligence when investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing funds. The test of whether the standard is met is if a prudent person acting in such a situation would engage in similar conduct to ensure investments safeguard principal and maintain liquidity.

PUT OPTION – The sale of an option to another party giving them the right to sell to the Investment Pool a security at a specified price within a specified time period.

RATING – Evaluation of financial institutions' investment and credit risks by professional rating services.

REGISTERED STATE WARRANT – A short-term obligation of a state governmental body issued in anticipation of revenue.

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) - 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.

SAFEKEEPING – A custodian bank’s action to store and protect an investor’s securities by segregating and identifying the securities.

SECURITIES AND EXCHANGE COMMISSION (SEC) – Agency created by Congress to protect investors in securities transactions by administering securities laws. The statutes administered by the SEC are designed to promote full public disclosure and protect the investing public against malpractice in the securities market.

SECURITIES LENDING – A transaction wherein the Investment Pool transfers its securities to broker/dealers and other entities for collateral which may be cash or securities and simultaneously agrees to return the collateral for the same securities in the future.

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

SHORT-TERM – A security with a maturity one year or less.

STANDARD AND POOR'S CORPORATION (S&P) – One of the three best known rating agencies in the United States, the others being Moody's Investment Service, Inc. (Moody's), and Fitch IBCA, Inc. (Fitch).

SWAP - Trading one asset for another.

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. This is calculated by taking the following components during a certain time period. (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 weekly, while auctions of one-year bills are 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 10 years and issued in denominations ranging from \$1,000 to \$1 million 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.

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

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 Curve - A graphic representation that depicts the relationship at a given point in time between yields and maturity for bonds that are identical in every way except maturity. A normal yield curve may be alternatively referred to as a positive yield curve.

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.