

EXHIBIT A
Revised Statement of Investment Policy
Fiscal Year 2023-2024

POLICY

The purpose of this document is to outline the policy on the investment of public monies.

It is the policy of the **City of Upland** and the **Successor Agency to the Upland Redevelopment Agency** (hereafter referred to collectively as the "City") to predicate their investment policies, procedures, and practices upon the limitations placed upon them by governing legislative bodies. These policies shall have three primary goals:

- To assure compliance with federal, state, and local laws governing the investment of public monies under the control of the City Treasurer.
- To protect the principal monies entrusted to the City.
- To generate the maximum amount of investment income within the parameters of prudent risk management as defined in this *Statement of Investment Policy*.

For the purposes of this policy, "Investment Officers" shall be defined as the City Treasurer, City Manager, Assistant City Manager, and the Finance Officer.

1.0 Scope

This *Statement of Investment Policy* shall apply to all funds that are under the control of the Investment Officers including, but not limited to, the general fund; special revenue funds; debt service funds; capital project funds; enterprise funds; trust and agency funds; and any other funds under the control of the Investment Officers. These funds are accounted for in the City's Annual Comprehensive Financial Report.

Investment of bond proceeds and related reserve funds shall be governed by the documents authorizing the issuance of such indebtedness. If the bond documents are silent as to the permitted investments, the bond proceeds will be invested in the securities permitted by this *Statement of Investment Policy*. Notwithstanding the other provisions of this *Statement of Investment Policy*, the percentage limitations listed in elsewhere in this *Statement of Investment Policy* do not apply to bond proceeds.

The City's Deferred Compensation Plan ("Plan") shall be excluded from the scope of this *Statement of Investment Policy* if: (1) a third-party administrator manages the Plan; (2) individual plan participants have control over the selection of investments; and (3) the City has no fiduciary responsibility to act as a "trustee" for the Plan. The only exception to the foregoing shall be that if the City retains the fiduciary responsibility to act as a trustee for the Plan, then the provisions of this *Statement of Investment Policy* shall apply to the investment of Plan assets. Under these circumstances, the Investment Officers shall provide the Finance Committee and the City Council with a quarterly report on the investment of Plan assets.

2.0 Standard of Care

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

Investment Officers who follow the provisions of this *Statement of Investment Policy*, and who exercise due diligence shall be relieved of personal responsibility for a security's credit risk or market price risk provided that they report substantial deviations from expectations to the City Manager and to the Finance Committee in a timely manner and that they take appropriate action to control adverse developments. "Substantial deviations" shall be defined as either a decline of 10 percent or more in the market value of a security due to issuer default or a credit risk downgrade or the premature sale of a security at 10 percent or more below its acquisition cost.

3.0 Objective

The City's investment objectives, in order of priority, shall be:

- 3.1 **Safety.** Safety of principal shall be the foremost objective. Investments shall be made with the aim of avoiding capital losses due to issuer default; broker-dealer default; or market value erosion. Principal shall be preserved by mitigating:
 - 3.1.1 **Credit Risk**, the risk of loss due to the failure of the issuer of the security, shall be mitigated by investing in only high-quality securities and by diversifying investments; and
 - 3.1.2 **Market Risk**, the risk of loss due to a decline in bond prices because of rising market interest rates, shall be mitigated by structuring the portfolios so that issues mature concurrently with the City's anticipated cash requirements, thereby eliminating the need to sell securities prematurely on the open market.
 - 3.1.3 It is recognized, however, that in a diversified portfolio, occasional measured losses are inevitable and must be considered within the context of the overall investment strategy.
- 3.2 **Liquidity.** An adequate percentage of the portfolios shall be maintained in liquid, short-term securities that can be converted to cash, if necessary, to meet disbursement requirements. Since all cash requirements cannot be anticipated, the portfolios should

consist largely of securities with active secondary markets. These securities should have a relatively low sensitivity to market risk. Maximum overall portfolio maturities are referenced in section 15.0, paragraph 2 of this *Statement of Investment Policy*.

3.3 Yield. Yield shall be considered only after the basic requirements of safety and liquidity have been met.

4.0 Delegation of Authority

California Government Code (“Code”) Sections 53607 and 53608 authorize the legislative body of a local agency to invest, deposit, and provide for the safekeeping of the local agency 's funds or to delegate those responsibilities to the treasurer of the local agency. The delegation of investment authority by the City Council to the Investment Officers shall be for a period of one-year period, unless revoked. Subject to review, the City Council may renew the delegation of authority each year.

The Investment Officers shall have the exclusive authority to buy and sell securities on behalf of the City. They shall engage in mutual consultation and in collective decision making on economic trends, investment opportunities, and portfolio structuring.

5.0 Internal Controls

The Investment Officers shall be responsible for ensuring that all investment transactions comply with the City’s *Statement of Investment Policy* and for establishing internal controls that are designed to prevent losses due to fraud, negligence, and third-party misrepresentation. The Investment Officers shall establish written procedures for the operation of the City’s investment program that are consistent with this *Statement of Investment Policy*.

Internal controls deemed most important shall include: avoidance of collusion; separation of duties and administrative controls; separating transaction authority from accounting and record keeping; custodial safekeeping; clear delegation of authority; management approval and review of investment transactions; specific limitations regarding securities losses and remedial action; written confirmation of telephone transactions; documentation of investment transactions and strategies; and monitoring of results.

6.0 Conflict of Interest

Investment Officers shall refrain from personal business activity that could conflict with the proper execution of the City's investment program or impair their ability to make impartial investment decisions. They shall disclose to the City Council any material financial interest in financial institutions that conduct business within the City's jurisdiction. They shall also disclose any personal investment positions that could be related to the performance of the City's investment portfolios. Investment Officers shall subordinate their personal investment transactions to those of the City, particularly with regard to the timing of securities purchases and sales, and shall avoid transactions that might impair public confidence.

Investment Officers and their immediate relatives shall not accept or solicit any gifts, gratuities, honorariums, or favors from persons or entities who provide or who are seeking to provide financial services to the City.

7.0 Authorized Broker-Dealers

The Investment Officers shall have the authority to select any issuer, or qualified broker-dealer(s) deemed necessary in facilitating investment transactions.

For securities not purchased directly from the issuer, the Investment Officers will maintain a list of approved financial institutions authorized to provide investment services to the City in the State of California. These may include “primary” dealers or regional dealers that qualify under Securities & Exchange Commission Rule 15C3-1 (uniform net capital rule). Best practices include the following: 1) A determination that all approved broker/dealer firms, and individuals covering the City, are reputable and trustworthy; 2) the broker/dealer firms should have the ability to meet all their financial obligations in dealing with the City; 3) the firms, and individuals covering the agency, should be knowledgeable and experienced in public agency investing and the investment products involved; 4) no public deposit shall be made except in a qualified public depository as established by the established State laws; 4) all financial institutions and broker/dealers who desire to conduct investment transactions with the City may supply the Investment Officers with audited financial statements, proof of FINRA certification, trading resolution, proof of State of California registration, a completed broker/dealer questionnaire, certification of having read the City’s investment policy and depository contracts.

An annual review of the financial condition and registrations of qualified broker/dealer firms may be conducted by the City and a current audited financial statement requested for each financial institution and broker/dealer in which the City invests. In addition to other requirements, the Investment Officers shall give all approved broker-dealers a copy of the City’s current *Statement of Investment Policy* and a certification form. The completion and submission of the certification form by an approved broker-dealer shall constitute proof that it has received the City's *Statement of Investment Policy*, read it, and intends to comply with it. The Investment Officers shall keep current audited annual financial statements on file for each approved broker-dealer with which the City does business.

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, the investment officer shall make their best efforts to document quotations for comparable or alternative securities.

8.0 Authorized Public Depositories

The Investment Officers shall maintain an Approved List of all financial institutions that the Finance Committee and the City Council have authorized as public depositories of City monies. This List shall be provided to all members of the City Council and the Finance Committee.

The City shall only deposit public monies in financial institutions that have: (1) an overall Community Reinvestment Act rating of not less than “satisfactory” of meeting the credit needs of California’s communities; (2) at least \$100 million in total assets; (3) a core capital-to-total assets ratio of at least five percent; (4) favorable statistical ratings from a nationally recognized rating service, as determined by the Investment Officers; (5) a federal or a state charter; and (6) a branch office within San Bernardino County and/or Los Angeles County.

Under no circumstances shall the City's deposits in a financial institution exceed the total shareholder's equity of that institution.

Any financial institution that has City funds on deposit must comply with the requirements of Code Sections 53630 *et seq.*, including collateralization of deposits. The Investment Officers may waive the collateralization requirements for any portion of the deposit that is covered by Federal Deposit Insurance. As provided by Code Section 53649, the City shall have a signed contract with each financial institution that has City funds on deposit.

9.0 Safekeeping and Custody

Investment Officers shall conduct all security transactions on a delivery-versus-payment ("DVP") or on a receipt-versus-payment ("RVP") basis. A third-party bank trust department ("Custodian") that acts as an agent for the City under the terms of a custody agreement executed between both parties shall hold the securities. The City's Custodian shall be represented on the Approved List.

The only exception to the foregoing shall be securities purchases made with: (1) local government investment pools; (2) money market mutual funds; and (3) Federal Reserve Banks ("Treasury Direct Program") since the purchased securities are not deliverable. No securities broker-dealer or investment advisor shall have access to City monies, accounts, or investments. Any transfer of monies to or through a securities broker-dealer must have the Investment Officers' prior written approval. If they are unavailable, then the management authorization chain-of-command specified in section 4.0, paragraph 2 of this *Statement of Investment Policy* shall be followed.

The City shall not purchase more than \$15 million of securities from the Custodian if the Custodian will subsequently be holding those securities in custody for the City.

The City shall require Broker Trade Confirmations for all trades. Investment Officers shall review these confirmations immediately upon receipt, for conformity with the terms of the City's Trade Sheets.

10.0 Authorized Investments

The City's investments are governed by Code, Sections 53600 *et seq.* Within the investments permitted by the Code, the City seeks to further restrict eligible investments to the guidelines listed below. In the event a discrepancy is found between this *Statement of Investment Policy* and the Code, the more restrictive parameters will take precedence. Percentage holding limits listed in this section apply at the time the security is purchased.

Any investment currently held at the time this *Statement of Investment 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 financial institutions.

10.01 United States Instruments

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. *There is no limitation as to the percentage of City's investment portfolio that may be invested in this category.*

10.02 Federal Agency Securities

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. *There is no limitation as to the percentage of City's investment portfolio that may be invested in this category. No more than 50 percent of the market value of the City's investment portfolio may be invested in any one issuer. No more than 50 percent of the market value of the City's investment portfolio may be invested in callable securities.*

10.03 Municipal Securities

Bonds issued by the City, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the City or by a department, board, agency, or authority of the City. Purchases of any obligation of the City of Upland by an Enterprise Fund of the City shall not require a rating from a Nationally Recognized Statistical Rating Organization (NRSRO).

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.

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.

Bonds, notes, warrants, or other evidences of indebtedness of a 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.

Purchases are limited to securities rated in a rating category of "A" (long-term) or "A-1" (short-term) or their equivalents or better by a NRSRO. *No more than 30 percent of the market value of the City's investment portfolio shall be invested in this category.*

10.04 Medium-Term Notes

Defined as all corporate and depository institutions debt securities with 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. Investment shall be limited to medium-term notes ("MTN") rated in a rating category of "A" or better by an NRSRO. *No more than 30 percent of the market value of the City's investment portfolio shall be invested in this category.*

10.05 Bankers' Acceptances

Bankers' acceptances (BAs) otherwise known as bills of exchange or time drafts that are drawn on and accepted by a commercial bank which have short-term debt obligations rated in the rating category of "A-1" or higher by a NRSRO. Purchases of BAs shall not exceed 180 days to maturity. *No more than 40 percent of the market value of the City's investment portfolio shall be invested in this category.*

10.06 Commercial Paper

Commercial paper of "prime" quality of the highest ranking or of the highest letter and number rating as provided for by a NRSRO. The entity that issues the commercial paper shall meet 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), and (C) Has debt other than commercial paper, if any, that is rated in a rating category of "A" or its equivalent or better by an NRSRO. *Purchases of CP shall not exceed 270 days to maturity. No more than 40 percent of the market value of the City's investment portfolio shall be invested in this category. If the City's investable assets fall below \$100 million, no more than 25 percent of the market value of the City's investment portfolio shall be invested in this category.*

10.07 Asset Backed, Mortgage-Backed, Mortgage Pass-Through securities and Collateralized Mortgage Obligations

A mortgage passthrough security, collateralized mortgage obligation, mortgage-backed or other pay-through bond, equipment lease-backed certificate, consumer receivable passthrough certificate, or consumer receivable-backed bond with a maximum remaining maturity of five years or less. Securities shall be rated in a rating category of "AA" or its equivalent or better by an NRSRO. *No more than 20 percent of the market value of the City's investment portfolio shall be invested in this category.*

10.08 Negotiable Certificates of Deposit

Negotiable certificates of deposit 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. Purchases are limited to securities rated in a rating category of "A" (long-term) or "A-1" (short-term) or their equivalents or better by an NRSRO. The Investment Officers can exempt from these rating requirements any Negotiable CDs for which the full amount of the CD

and the interest that may accrue shall at all times be covered by Federal Deposit insurance. *No more than 30 percent of the market value of the City's investment portfolio shall be invested in this category.*

10.09 Money Market Mutual Funds

Money Market Mutual Funds investments shall be permitted in shares of beneficial interest issued by diversified management companies that are government money market funds ("MMF") registered with the SEC under the Investment Company Act of 1940. Commission (e.g., sales load on purchases, reinvested dividends, redemptions, and exchanges) shall not be included in the purchase of any fund shares. A qualifying MMF must have: (1) total portfolio net assets of \$500 million or more; and (2) the highest rating of the two largest nationally recognized rating services OR an investment advisor who is registered with the SEC, and who has five years or more of experience investing for MMFs of \$500 million or more in total portfolio net assets. The City shall require audited annual financial statements from each MMF in which it has public monies invested. *No more than 20 percent of the market value of the City's investment portfolio may be invested in this category.*

10.10 Local Agency Investment Fund ("LAIF")

Investment shall be permitted in this pool which is organized and managed by the State Treasurer's Office for the benefit of local agencies, pursuant to Code Section 16429.1. The City Council approved City participation in LAIF on February 22, 1977 in Resolution Number 2716. The Successor Agency to the Redevelopment Agency approved participation in LAIF on February 13, 2012 in Resolution Number 2012-4. *Investment shall be limited to the maximum amount per legal entity that is permitted by the program.*

10.11 Supranational Securities

United States 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 shall be rated in a rating category of "AA" or its equivalent or better by a NRSRO. *No more than 30 percent of the market value of the City's investment portfolio may be invested in this category. No more than 10 percent of the market value of the City's investment portfolio may be invested in any single issuer, and the maximum maturity shall not exceed five years.*

10.12 Local Government Investment Pools ("LGIP").

Shares of beneficial interest issued by a joint powers authority organized pursuant to Section 6509.7 that invests in the securities and obligations authorized by Code. The City will limit investments to LGIPs that seek to maintain a stable net asset value. *There is no limitation as to the percentage of City's investment portfolio that may be invested in this category.*

10.13 Placement Service Deposits.

Funds may be placed with a California financial institution that may utilize a private sector entity that assists in the placement of deposit with eligible financial institutions located in the United States in accordance with Code 53601.8. The full amount of the principal and the interest that may be accrued during the maximum term of the deposit shall always be insured by federal deposit insurance. *No more than 30 percent of the market value of the City's investment portfolios may be invested in this category. The maximum investment maturity will be restricted to five years.*

10.14 Bank Deposits.

FDIC insured or fully collateralized demand deposit accounts, savings accounts, market rate accounts, or time certificates of deposits in financial institutions located in California. *There is no limitation as to the percentage of City's investment portfolio that may be invested in this category, however, no more than 25 percent of the market value of the portfolio may be invested in time deposits. The maximum investment maturity will be restricted to five years.*

11.0 Prohibited Investments and Practices

Investment Officers shall not invest public monies in financial instruments that are not authorized under this *Statement of Investment Policy*.

Prohibited investments shall include, but shall not be limited to, equity securities, bond mutual funds, repurchase agreements, reverse repurchase agreements, and derivative contracts (forwards, futures, and options). The purchase of derivative securities shall be prohibited *except for callable and for zero coupon Treasury ("STRIPS") securities.*

Investment Officers shall not engage in securities lending, short selling, or other hedging strategies.

LAIF, LGIPs, and MMFs shall be exempt from the prohibitions on derivative contracts, derivative securities, repurchase agreements, reverse repurchase agreements, securities lending, short selling, and other hedging strategies.

12.0 Investment Pools

Investment Officers shall investigate all investment pools (LAIF, LGIPs, MMFs) prior to investing public monies and periodically thereafter while City public monies are invested in the investment pool.

13.0 Diversification

Investment Officers shall diversify the City's investment portfolio by security type and by issuer to avoid incurring unreasonable risks inherent in over-investing in specific instruments, individual financial institutions, or maturities. No more than 5 percent of the total portfolio market value may be invested in securities of any single issuer, except where the issuer is the US Government, its Agencies and GSEs, supranational securities, collateralized deposits,

LAIF, money market mutual funds or local government investment pools.

14.0 Maximum Maturity

For those investment types for which this *Statement of Investment Policy* does not specify a maturity limit, no individual investment shall exceed a maturity of five years from the date of purchase unless the City Council has granted express authority to make that investment either specifically or as a part of an investment program approved by the City Council no less than three months prior to the investment.

Additionally, the City may purchase a Municipal Security issued by the City from surplus moneys of any fund of the City as a part of an investment program approved by the legislative body no less than three months prior to the investment. This would include investments made to reduce the City's Unfunded Accrued Liability (UAL) with California Public Employees' Retirement System (CalPERS).

This Policy authorizes investing bond project and reserve funds beyond five years if the maturities of such investments do not exceed the expected use of the funds, the investments are deemed prudent in the opinion of the Investment Officers, and the investments are not prohibited by the applicable bond documents.

Maturities may vary from 1 day to five years at the investment officers' discretion. Municipal Securities of the City to reduce its UAL with CalPERS may have a maturity up to and not exceeding twenty years, and which shall be approved by the City Council. The portfolio should be managed in such a manner as to meet the City's liquidity, safety, and capital preservation needs.

15.0 Portfolio Rebalancing

In the event that portfolio percentage constraints are violated due to a temporary imbalance in the portfolio, then Investment Officers may hold the affected securities to maturity in order to avoid capital losses. If no capital losses would be realized upon sale, however, then the Investment Officers shall consider rebalancing the portfolio after evaluating the expected length of time that it will be imbalanced. Portfolio percentage limits are in place in order to ensure diversification of the City investment portfolio; a small, temporary imbalance, not to exceed three months, will not significantly impair that strategy. Bond or note proceeds shall not be factored into the balance of the portfolio.

16.0 Credit Downgrading

This *Statement of Investment Policy* sets forth minimum credit risk criteria for each type of security. This credit risk criteria applies to the initial purchase of a security; it does not automatically force the sale of a security if its credit risk ratings fall below policy limits.

If a security is downgraded below the minimum credit risk criteria specified in this *Statement of Investment Policy*, then the Investment Officers shall evaluate the downgrade on a case-by-case basis in order to determine if the security should be held or sold.

The Investment Officers shall inform the Finance Committee at its next regular meeting of the credit downgrade and of the Investment Officer's decision to hold or sell the downgraded

security.

The Investment Officers shall review the credit standing of all securities in the City's investment portfolios on a semiannual basis.

17.0 Portfolio Benchmark

The City Treasurer shall monitor and evaluate the portfolio's performance relative to a market benchmark, which will be included in the Treasurer's monthly report. The City Treasurer shall select an appropriate, readily available index to use as a market benchmark.

The City's portfolios may be actively managed for purposes of improving portfolio risk structure, liquidity, or yield in response to market conditions or to meet City requirements.

18.0 Reporting

The Investment Officers shall provide a monthly report of investment transactions to the City Council and an investment report to the Finance Committee at the regularly scheduled meeting.

The investment report shall include a complete portfolio inventory with details on issue, par value, market value, coupon/rate, original settlement date of purchase, final maturity date, average weighted yield, and average days to maturity, and market value (including source of market valuation). The report will include a statement on compliance or noncompliance with the City's *Statement of Investment Policy* and a statement on whether there are or are not sufficient funds to meet the City's anticipated cash requirements for the next six months.

19.0 Policy Review and Adoption

The Investment Officers shall submit a *Statement of Investment Policy*, including any recommended changes, to the City Council and the Successor Agency Board annually for their review and adoption.

GLOSSARY OF INVESTMENT TERMS

Agencies. Shorthand market terminology for any obligation issued by a *government-sponsored entity (GSE)*, or a *federally related institution*. Most obligations of GSEs are not guaranteed by the full faith and credit of the US government. Examples are:

FFCB. The Federal Farm Credit Bank System provides credit and liquidity in the agricultural industry. FFCB issues discount notes and bonds.

FHLB. The Federal Home Loan Bank provides credit and liquidity in the housing market. FHLB issues discount notes and bonds.

FHLMC. Like FHLB, the Federal Home Loan Mortgage Corporation provides credit and liquidity in the housing market. FHLMC, also called "Freddie Mac" issues discount notes, bonds, and mortgage pass-through securities.

FNMA. Like FHLB and Freddie Mac, the Federal National Mortgage Association was established to provide credit and liquidity in the housing market. FNMA, also known as "Fannie Mae," issues discount notes, bonds, and mortgage pass-through securities.

GNMA. The Government National Mortgage Association, known as "Ginnie Mae" issues mortgage pass-through securities, which are guaranteed by the full faith and credit of the US Government.

PEFCO. The Private Export Funding Corporation assists exporters. Obligations of PEFCO are not guaranteed by the full faith and credit of the US government.

TVA. The Tennessee Valley Authority provides flood control and power and promotes development in portions of the Tennessee, Ohio, and Mississippi River valleys. TVA currently issues discount notes and bonds.

Asked. The price at which a seller offers to sell a security.

Asset Backed Securities. Securities supported by pools of installment loans or leases or by pools of revolving lines of credit.

Average Life. In mortgage-related investments, including CMOs, the average time to expected receipt of principal payments, weighted by the amount of principal expected.

Bankers' Acceptance. A money market instrument created to facilitate international trade transactions. It is highly liquid and safe because the risk of the trade transaction is transferred to the bank which "accepts" the obligation to pay the investor.

Benchmark. A comparison security or portfolio. A performance benchmark is a partial market index, which reflects the mix of securities allowed under a specific investment policy.

Bid. The price at which a buyer offers to buy a security.

Broker. A broker brings buyers and sellers together for a transaction for which the broker receives a commission. A broker does not sell securities from his own position.

Callable. A callable security gives the issuer the option to call it from the investor prior to its maturity. The main cause of a call is a decline in interest rates. If interest rates decline since an issuer issued a security, the issuer will likely call its current securities and reissue them at a lower rate of interest. Callable securities have reinvestment risk as the investor may receive its principal back when interest rates are lower than when the investment was initially made.

Certificate of Deposit (CD). A time deposit with a specific maturity evidenced by a certificate. Large denomination CDs may be marketable.

Collateral. Securities or cash pledged by a borrower to secure repayment of a loan or repurchase agreement. Also, securities pledged by a financial institution to secure deposits of public monies.

Collateralized Mortgage Obligations (CMO). Classes of bonds that redistribute the cash flows of mortgage securities (and whole loans) to create securities that have different levels of prepayment risk, as compared to the underlying mortgage securities.

Commercial Paper. The short-term unsecured debt of corporations.

Cost Yield. The annual income from an investment divided by the purchase cost. Because it does not give effect to premiums and discounts which may have been included in the purchase cost, it is an incomplete measure of return.

Coupon. The annual rate of interest which is paid on a bond.

Credit Risk. The risk that principal and/or interest on an investment will not be paid in a timely manner due to changes in the condition of the issuer.

Current Yield. The annual income from an investment divided by the current market value. Since the mathematical calculation relies on the current market value rather than the investor's cost, current yield is unrelated to the actual return the investor will earn if the security is held to maturity.

Dealer. A dealer acts as a principal in security transactions, selling securities from and buying securities for his own position.

Debenture. A bond secured only by the general credit of the issuer.

Delivery vs. Payment (DVP). A securities industry procedure whereby payment for a security must be made at the time the security is delivered to the purchaser's agent.

Derivative. Any security that has principal and/or interest payments which are subject to uncertainty (but not for reasons of default or credit risk) as to timing and/or amount, or any security which represents a component of another security which has been separated from other components ("Stripped" coupons and principal). A derivative is also defined as a financial instrument the value of which is totally or partially derived from the value of another instrument, interest rate, or index.

Discount. The difference between the par value of a bond and the cost of the bond, when the cost is below par. Some short-term securities, such as T-bills and banker's acceptances, are known as **discount securities**. They sell at a discount from par and return the par value to the investor at maturity without additional interest. Other securities, which have fixed coupons, trade at a discount when the coupon rate is lower than the current market rate for securities of that maturity and/or quality.

Diversification. Dividing investment funds among a variety of investments to avoid excessive exposure to any one source of risk.

Duration. The weighted average time to maturity of a bond where the weights are the present values of the future cash flows. Duration measures the price sensitivity of a bond to changes in interest rates. (See modified duration).

Federal Deposit Insurance Corporation (FDIC). An independent US agency that insures bank deposits, including deposits in a checking account, negotiable order of withdrawal (NOW) account savings account, money market deposit account (MMDA), time deposit such as a certificate of deposit (CD), or an official item issued by a bank (such as a cashier's check or money order), currently up to \$250,000 per depositor, per issued bank, for each account ownership category.

Federal Funds Rate. The rate of interest charged by banks for short-term loans to other banks. The Federal Reserve Bank through open-market operations establishes it.

Federal Open Market Committee. A committee of the Federal Reserve Board that establishes monetary policy and executes it through temporary and permanent changes to the supply of bank reserves.

Investment Advisor. As defined by the Investment Advisors Act of 1940, any person or group that makes investment recommendations or conducts securities analysis in return for a fee, whether through direct management of client assets or via written publications. An investment advisor who has sufficient assets to be registered with the SEC is known as a Registered Investment Advisor, or RIA. Investment advisors are prohibited from disseminating advice known to be deceitful or fraudulent and from acting as a principal on their own accounts by buying and selling securities between themselves and a client without prior written consent.

Leverage. Borrowing funds in order to invest in securities that have the potential to pay earnings at a rate higher than the cost of borrowing.

Liquidity: The speed and ease with which an asset can be converted to cash without a substantial loss in value

Local Agency Investment Fund (LAIF). The aggregate of all funds from political subdivisions that are placed in custody of the State Treasurer for investment and reinvestment.

Local Government Investment Pool (LGIP). A comingled investment pool comprised of funds from political subdivisions that are placed in custody of the program for investment and reinvestment.

Make Whole Call. A type of call provision on a bond that allows the issuer to pay off the remaining debt early. Unlike a call option, with a make whole call provision, the issuer makes a lump sum payment that equals the net present value (NPV) of future coupon payments that will not be paid because of the call. With this type of call, an investor is compensated, or "made whole."¹¹

Margin: The difference between the market value of a security and the loan a broker makes using that security as collateral.

Market Risk. The risk that the value of securities will fluctuate with changes in overall market conditions or interest rates.

Market Value. The price at which a security can be traded.

Marking to Market. The process of posting current market values for securities in a portfolio.

Maturity. The final date upon which the principal of a security becomes due and payable.

Medium Term Notes. Unsecured, investment-grade senior debt securities of major corporations which are sold in relatively small amounts on either a continuous or an intermittent basis. MTNs are highly flexible debt instruments that can be structured to respond to market opportunities or to investor preferences.

Modified Duration. The percent change in price for a 100 basis point change in yields. Modified duration is the best single measure of a portfolio's or security's exposure to market risk.

Money Market. The market in which short-term debt instruments (T-bills, discount notes, commercial paper, and banker's acceptances) are issued and traded.

Mortgage Pass-Through Securities. A securitized participation in the interest and principal cash flows from a specified pool of mortgages. Principal and interest payments made on the mortgages are passed through to the holder of the security.

Municipal Securities. Securities issued by state and local agencies to finance capital and operating expenses.

Mutual Fund. An entity which pools the funds of investors and invests those funds in a set of securities which is specifically defined in the fund's prospectus. Mutual funds can be invested

in various types of domestic and/or international stocks and bonds, and money market instruments, as set forth in the individual fund's prospectus. For most large, institutional investors, the costs associated with investing in mutual funds are higher than the investor can obtain through an individually managed portfolio.

Nationally Recognized Statistical Rating Organization (NRSRO). A credit rating agency that the Securities and Exchange Commission in the United States uses for regulatory purposes. Credit rating agencies provide assessments of an investment's risk. The issuers of investments, especially debt securities, pay credit rating agencies to provide them with ratings. The three most prominent NRSROs are Fitch, S&P, and Moody's.

Premium. The difference between the par value of a bond and the cost of the bond, when the cost is above par.

Prepayment Speed. A measure of how quickly principal is repaid to investors in mortgage securities.

Prepayment Window. The time period over which principal repayments will be received on mortgage securities at a specified prepayment speed.

Primary Dealer. A financial institution (1) that is a trading counterparty with the Federal Reserve in its execution of market operations to carry out U.S. monetary policy, and (2) that participates for statistical reporting purposes in compiling data on activity in the U.S. Government securities market.

Prudent Person (Prudent Investor) Rule. A standard of responsibility which applies to fiduciaries. In California, the rule is stated as "Investments shall be managed with the care, skill, prudence and diligence, under the circumstances then prevailing, that a prudent person, acting in a like capacity and familiar with such matters, would use in the conduct of an enterprise of like character and with like aims to accomplish similar purposes."

Realized Yield. The change in value of the portfolio due to interest received and interest earned and realized gains and losses. It does not give effect to changes in market value on securities, which have not been sold from the portfolio.

Regional Dealer. A financial intermediary that buys and sells securities for the benefit of its customers without maintaining substantial inventories of securities and that is not a primary dealer.

Repurchase Agreement (RP, Repo). Short-term purchases of securities with a simultaneous agreement to sell the securities back at a higher price. From the seller's point of view, the same transaction is a reverse repurchase agreement.

Safekeeping. A service to bank customers whereby securities are held by the bank in the customer's name.

Structured Note. A complex, fixed income instrument, which pays interest, based on a formula tied to other interest rates, commodities, or indices. Examples include inverse floating rate notes which have coupons that increase when other interest rates are falling, and which fall when other interest rates are rising, and "dual index floaters," which pay interest based on the

relationship between two other interest rates - for example, the yield on the ten-year Treasury note minus the Libor rate. Issuers of such notes lock in a reduced cost of borrowing by purchasing interest rate swap agreements.

Supranational. A Supranational is a multi-national organization whereby member states transcend national boundaries or interests to share in the decision making to promote economic development in the member countries.

Time Deposit. A savings account or certificate of deposit (CD) that pays a fixed rate of interest until a given maturity date.

Total Rate of Return. A measure of a portfolio's performance over time. It is the internal rate of return, which equates the beginning value of the portfolio with the ending value; it includes interest earnings, realized and unrealized gains, and losses in the portfolio.

U.S. Treasury Obligations. Securities issued by the U.S. Treasury and backed by the full faith and credit of the United States. Treasuries are considered to have no credit risk and are the benchmark for interest rates on all other securities in the US and overseas. The Treasury issues both discounted securities and fixed coupon notes and bonds.

Treasury Bills. Treasury securities issued with initial maturities of one year or less are issued as discounted instruments and are called Treasury bills. The Treasury currently issues three- and six-month T-bills at regular weekly auctions. It also issues "cash management" bills as needed to smooth out cash flows.

Treasury Notes. Treasury securities issued with initial maturities of two to ten years are called Treasury notes and pay interest semi-annually.

Treasury Bonds. Treasury securities issued with initial maturities greater than ten years are called Treasury bonds. Like Treasury notes, they pay interest semi-annually.

Volatility. The rate at which security prices change with changes in general economic conditions or the general level of interest rates.

Yield to Maturity. The annualized internal rate of return on an investment which equates the expected cash flows from the investment to its cost.