RESOLUTION NO. 6546

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF UPLAND APPROVING AND ADOPTING THE ANNUAL STATEMENT OF INVESTMENT POLICY FOR FISCAL YEAR 2020-21

Intent of the Parties and Findings

(i) Government Code Section 53646 of the State of California requires the City Treasurer or the Chief Fiscal Officer to render an annual statement of investment policy which must be considered at a public meeting; and

(ii) Government Code Section 53600 et seq., provides guidelines and regulations pertaining to investment of temporary idle funds.

NOW, THEREFORE, the City Council hereby finds, determines and resolves as follows:

Section 1. City Council does hereby adopt the attached Exhibit A containing the Statement of Investment Policy for the fiscal year 2020-21.

Section 2. Any and all prior resolutions adopting a Statement of Investment Policy for the City of Upland shall be hereby rescinded.

Section 3. Certification. The City Clerk shall certify to the passage and adoption of this resolution and enter it into the book of original resolutions.

PASSED, APPROVED and ADOPTED this 8th day of June, 2020.

Debbie Stone

Debbie Stone, Mayor

I, Keri Johnson, City Clerk of the City of Upland, do hereby certify that the foregoing Resolution was adopted at a regular meeting of the City Council held on the 8th day of June, 2020, by the following vote:

AYES: Mayor Stone, Councilmembers Elliott, Velto, Zuniga
NOES: None
ABSENT: None
ABSTAINED: None

ATTEST:

Keri Johnson, City Clerk

EXHIBIT A

POLICY NO.: 2
SUBJECT: "STATEMENT OF INVESTMENT POLICY"
Dated: June 8, 2020

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 City Treasurer 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 City Treasurer. These funds are accounted for in the City's Comprehensive Annual Financial Report.

Investment of bond proceeds and related reserve funds shall be governed by the documents authorizing the issuance of such indebtedness.

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 Finance Officer shall provide the Investment 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 Investment 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 Objectives

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 the highest 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 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 City Treasurer, City Manager, Assistant City Manager or Finance Officer 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 City Treasurer and Finance Officer 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 City Treasurer and Finance Officer 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.

The Investment Committee consists of two City Council members, selected by the Mayor, and the City Treasurer. The Committee shall be responsible for reviewing changes to the City investment reports, transactions, policies and procedures, and strategies, on a quarterly basis.

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 Finance Officer or Assistant City Manager shall have the authority to select any qualified broker-dealer(s) deemed necessary in facilitating investment transactions.

Any broker-dealer that has made a political contribution within any consecutive four-year period following January 1, 1996 in an amount that exceeds the limits in Municipal Securities Rulemaking Board ("MSRB") Rule G-37, to any member of or candidate for the City Council or City Treasurer shall not be eligible to transact business with the City.

Qualified broker-dealers (1) have been in existence for more than five years; (2) have a net capital position in excess of $100 million; (3) are licensed as broker-dealers by the State of California; and (4) are headquartered or have a branch office in California.

The Finance Officer shall conduct an annual review of the financial condition and the registrations of all approved broker-dealers. In addition to other requirements, the City 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 Finance Officer 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 Finance Officer shall maintain an Approved List of all commercial banks 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) at least $100 million in total assets; (2) a core capital-to-total assets ratio of at least five percent; (3) favorable statistical ratings from a nationally recognized rating service, as determined by the City Treasurer; (4) a federal or a state charter; and (5) a branch office within San Bernardino County and/or Los Angeles County. The

only exception to the foregoing shall be 100% Federal Deposit Insurance Company (FDIC) insured securities purchased through a broker-dealer.

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

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 City Treasurer or Finance Officer's 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 Collateralization

Investment Officers shall ensure that all demand deposits and all non-negotiable certificates of deposit that exceed the FDIC insured limit, shall be fully collateralized with securities authorized under state law and under this *Statement of Investment Policy.* Collateral may be waived up to the FDIC limit for CD's since these will be insured by the FDIC. Any amount on deposit over the FDIC limit plus accrued interest, however, shall be collateralized with United States Treasury or federal agency securities at a constant margin ratio of 110 percent or with mortgage-backed collateral at a constant margin ratio of 150 percent.

Collateralized investments and demand deposits may require substitution of collateral. The City Treasurer must approve all requests from financial institutions for substitution of collateral that involve interchanging classes of security. An independent third party with whom the City has a current custodial agreement shall always hold the collateral. The independent third party shall provide the Finance Officer with a safekeeping receipt that he shall retain.

11.0 Authorized Investments

The City's investments are governed by California Government 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 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 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 financial institutions.

11.01 United States Treasury Bills, Notes, Bonds, and Certificates of Indebtedness

There shall be no concentration limit on the purchase of Treasuries other than for zero coupon securities. *Purchases of zero coupon Treasuries shall not exceed 10 percent of the market value of the City's investment portfolio.*

11.02 Federal Agency and Instrumentality Notes

Investment shall be permitted in the following discount and coupon security issuers: the Federal Farm Credit Bank, the Federal Home Loan Bank, the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, the Tennessee Valley Authority, the Export-Import Bank of the United States, the Federal Land Bank, the Small Business Administration, the Student Marketing Loan Association, and the Farm Credit Consolidated System. *Purchases of callable securities shall not exceed 50 percent of the market value of the City's investment portfolio. No more than 50 percent of the market value of the City's investment portfolios may be invested in any one issuer.*

11.03 Municipal Securities

Obligations of the City, the State of California, any of the other 49 states, and any local agency within the State of California. *Purchases must be rated in a rating category of "A"* or *higher by at least one nationally recognized statistical rating organization (NRSRO).*

11.04 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. *Purchases shall not exceed 30 percent of the market value of the City's investment portfolio.*

11.05 Bankers' Acceptances

Investment shall be permitted in prime banker' s acceptances ("BA") issued by commercial banks which have short-term debt obligations rated "A-1" or higher by at least one nationally recognized statistical-rating organization; or long-term debt obligations which are rated in a rating category of "A" or higher by at least one nationally recognized statistical rating organization. *Purchases of BAs shall not exceed 180 days to maturity. Purchases of BAs shall not exceed 40 percent of the market value of the City's investment portfolios. No more than 30 percent of the market value of the City's investment portfolios shall be invested in BAs issued by any one bank.*

11.06 Commercial Paper

Investment shall be permitted in prime commercial paper ("CP") that is rated "A" by an NRSRO. The issuing corporation must be organized and operating in the United States; have total assets of $500 million or more; and have long-term debentures that have been rated "A" or higher by a nationally recognized statistical rating organization. *Purchases of CP shall not exceed 270 days to maturity. No more than 15 percent of the market value of the City's investment portfolios shall be invested in CP. No more than 10 percent of the outstanding CP of any one issuer shall be purchased.*

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

The securities must be rated in a rating category of "AA" or higher by a nationally recognized statistical rating organization and are issued by corporations which have long-term obligations that are rated in a rating category of "A" or higher by at least one nationally recognized statistical rating organization. *No more than 20% of the total portfolio market value may be invested in these securities. There is no issuer limitation on any Mortgage security where the issuer is the US Treasury or a Federal Agency/GSE. The maximum maturity must not exceed five years.*

11.08 Certificates of Deposit

Investment shall be permitted in negotiable and non-negotiable, collateralized certificates of deposit ("CD") issued by public depositories that meet the criteria specified in section 8.0, paragraph 2 of this *Statement of Investment Policy.* CDs that exceed the FDIC insured limit shall be collateralized pursuant to the provisions of this *Statement of Investment Policy. No more than 30 percent of the market value of the City's investment portfolio shall be invested in CDs. If collateralization will not be involved, then no more than the maximum insured amount may be invested in any one issuer.*

11.09 Mutual Funds and Money Market Mutual Funds

Mutual Funds and Money Market Mutual Funds that are registered with the Securities and Exchange Commission under the Investment Company Act of 1940, provided:

Mutual Funds 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: (1) attained the highest ranking or the highest letter and numerical rating provided by not less than two NRSROs; and (2) 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. Commission (e.g., sales load on purchases, reinvested dividends, redemptions, and exchanges) shall not be included in the purchase of any fund shares. *No more than 10 percent of the total portfolio may be invested in shares of any one mutual fund. No more than 20 percent of the total portfolio may be invested in mutual funds and money market mutual funds.*

Money Market Mutual Funds investments shall be permitted in shares of beneficial interest issued by diversified management companies that are money market funds ("MMF") registered with the SEC under the Investment Company Act of 1940. In seeking to maintain a stable share price of $ 1.00, the MMF shall have a dollar-weighted average maturity of 90 days or less and shall purchase securities with an effective maturity of 13 months or less. 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 portfolios may be invested in mutual funds and*

MMFs.

11.10 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 California Government 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 under state law.*

11.11 Supranational Securities

Investment shall be permitted in issues that 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 shall be rated in a rating category of "AA" or its equivalent or better by a NRSRO. *No more than 30 percent of the total portfolio invested in these securities. No more than 10 percent of the portfolio may be invested in any single issuer, and the maximum maturity shall not exceed five years.*

12.0 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 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.

13.0 Investment Pools

Investment Officers shall investigate all local government investment pools ("LGIPs") prior to investing public monies and periodically thereafter while City public monies are invested in the LGIP. With the exception of LAIF, all LGIPs shall meet the criteria specified for money market funds in this *Statement of Investment Policy.*

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

15.0 Maximum Maturity

Investment Officers shall not invest in securities with maturities exceeding five years. The Investment Committee and City Council, however, may approve longer maturities for the investment of bond reserve, bond escrow, and other funds if the maturities of such investments are expected to coincide with the use of the funds.

Maturities may vary from 1 day to five years at the investment officers' discretion. The portfolio should be managed in such a manner as to to meet the City's liquidity, safety and capital preservation needs.

16.0 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.

17.0 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 Finance Officer 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.

18.0 Portfolio Benchmark

The Treasurer shall monitor and evaluate the portfolio's performance relative to market benchmark, which will be included in the Treasurer's monthly report. The 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.

19.0 Performance Reporting

The Finance Officer shall provide an investment report to the Investment Committee at the regularly scheduled meeting.

This 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.

20.0 Policy Review and Adoption

The City Treasurer and Finance Officer shall submit a *Statement of Investment Policy* 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 "FreddieMac" issues discount notes, bonds and mortgage pass-through securities.
>
> **FNMA.** Like FHLB and FreddieMac, the Federal National Mortgage Association was established to provide credit and liquidity in the housing market. FNMA, also known as "FannieMae" issues discount notes, bonds and mortgage pass-through securities.
>
> **GNMA.** The Government National Mortgage Association, known as "GinnieMae" 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 issues securities, it 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 Government Investment Pool (LGIP). The aggregate of all funds from political subdivisions that are placed in custody of the State Treasurer 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."

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

Treasury Bonds. All 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.