COUNCIL AGENDA: 09-28-10
ITEM: 3.3

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Lee Price, MMC
City Clerk

SUBJECT: PROPOSED REVISIONS TO CITY OF SAN JOSE INVESTMENT POLICY

DATE: 09-20-10

RECOMMENDATION

As recommended by the Public Safety, Finance and Strategic Support Committee on September 16, 2010 and outlined in the attached memo previously submitted to the Public Safety, Finance and Strategic Support Committee, accept the Annual Review and Proposed Amendments of the City's Investment Policy, and adopt a resolution approving revisions to City Council Policy 1-12, the City of San Jose Investment Policy, including but not limited to, clarifying technical terms, increasing portfolio diversification, and reducing portfolio concentration risk.

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: PUBLIC SAFETY, FINANCE AND STRATEGIC SUPPORT COMMITTEE

FROM: Scott P. Johnson

SUBJECT: **PROPOSED REVISIONS TO CITY OF SAN JOSÉ INVESTMENT POLICY**

DATE: September 8, 2010

Approved Deanna Santana Date 9/10/10

RECOMMENDATION

It is recommended that the Public Safety, Finance and Strategic Support Committee accept and approve the proposed revisions and enhancements to the City of San José's Investment Policy and direct staff to return to the City Council with the appropriate resolution and amended documents.

OUTCOME

Acceptance of this recommendation will provide further clarification to the City's Investment Policy and enhance the policy framework, better equipping City Staff to make prudent investment decisions thus achieving the City's public fund investment goals of safety, liquidity, and yield.

BACKGROUND

The City of San José's Investment Policy ("Investment Policy") requires an annual review and certification of the Investment Policy by the City Council. On December 8, 2009, the City Council approved the annual certification of the Investment Policy. In addition to the annual certification of the Investment Policy, the Finance Department is required to submit any proposed changes to the Public Safety, Finance and Strategic Support Committee for consideration and approval, prior to submission to the City Council for review and approval. The purpose of this memorandum is to present the culmination of a comprehensive Investment Policy review performed by the Finance Department in conjunction with the City's Investment Advisor, Main Street Capital Advisors, and review by the City Attorney's Office.

On June 7, 2007 Council approved recommendations contained in the Macias Consulting Group's Evaluation of the City's Investment Program which among other recommendations included the hiring of an Investment Advisor. On March 23, 2010 Council approved the selection of Main Street Capital Advisors (MSCA) to assist with the Investment Program's management of the City's investment portfolio. In addition to providing technical and strategic support, the scope of services with MSCA includes review of the Investment Program procedures and policies and providing recommendations to enhance and streamline the City's Investment Program. Aside from general consultative support provided by MSCA, the contract scope of services requires specific deliverables in the first year of the contract including, but not limited to; assistance in developing updated procedures for annual review of financial institutions/brokers/dealers, assistance in developing procedures for the addition/deletion of brokers/dealers, on-site training, and an assessment of existing utilization of City cash flow data.

The primary initial deliverable included in the scope of services was for the Investment Advisor to participate in an initial comprehensive review of the City's Investment Policy and thereafter provide assistance in the future annual review process of the City's Investment Policy.
After extensive discussion and review by the Finance Department, in collaboration with the City Attorney's Office and MSCA, staff recommends the changes, updates, and clarifications to the Investment Policy as outlined in this memorandum and the attached red-lined version of the updated Policy for the Committee's consideration and approval. If approved by the Committee, the proposed changes will be forwarded to the Council for final consideration and approval along with the appropriate resolution..

ANALYSIS

The City's current Investment Policy was reviewed and certified by the Association of Public Treasurers (APT) of the United States and Canada earlier this year and was recognized as one of only 21 governments nationwide to have its investment policy certified by the APT this year. The APT certification program was instituted to assist state and local governments in drafting or improving upon an existing investment policy and comparing submitted policies to the Associations "Model" investment policy. The proposed changes to the Investment Policy do not deviate from and continue to demonstrate the City's primary Investment Policy objectives of safety, liquidity, and yield. In addition to the aforementioned policy objectives, the proposed recommendations continue to conform to the investment provisions of the California Government Code, the Charter of the City of San Jose, and the San Jose Municipal Code. The Finance Department proposes the following recommendations to enhance what is already a nationally recognized model investment policy.

The general purpose of the following recommendations is to clarify technical terms, strengthen consistency, increase portfolio diversification, reduce portfolio concentration risk, and enhance the credit quality of the portfolio.

Subsequent to the Public Safety, Finance and Strategic Support Committee's review of the proposed changes to the Investment Policy, staff will reformat the Investment Policy to include additional subcategory numbering for ease of reference prior to submission to the full Council for consideration on September 28, 2010. The summary below outlines the key general and substantive policy recommendations included in the attached copy of the Investment Policy which has been marked to show the proposed changes from the current Investment Policy:

General Policy Recommendations

Replace subjective words and phrases with objective words and phrases.

- *Section 1.0 Policy* – Replaced "maximum yield" with "rate of return" to more accurately reflect the City's objectives. Maximum yield insinuates seeking the highest yield and potentially overshadows the other priorities of safety and liquidity.

Edit phrases to better clarify the Intention of the Investment Policy.

- *Section 7.0 Authorized Financial Dealers and Institutions* – Clarified requirements for authorized financial dealers and institutions, and added the phrase "who work directly with the City" to ensure that individual brokers conducting business on behalf of the City have Financial Industry Regulation Authority (FINRA) certification.

- *Section 2.0 Scope (section 2)* – Added language clarifying that bond proceeds held in various trust accounts are not subject to the percentage restrictions set forth in Section 8 of the Investment Policy.

Add language to clarify Authorized Investments.

- *Section 8.0 Authorized Investments (subsections 5, 8, and 12)* – Expanded the "A" rating to "A3, A-, or A- " to accurately reflect the "A" rating associated with each rating agency (Moody's, Standard & Poor's and Fitch, respectively). In addition, added language to ensure that if investments are rated by any of the three rating agencies they are not rated lower than "A3, A-, or A- " by any of them.

Modify language to conform to current financial market conditions.

- *Section 8.0 Authorized Investments (subsection 2) - Federal Agencies* - Deleted reference to SLMA (Student Loan Marketing Association) since it was privatized several years ago and is no longer considered a Government Agency.

- *Section 8.0 Authorized Investments (subsection 10) - Money Market Mutual Funds* – Added language to clarify Money Market Mutual Funds' adherence to the Securities and Exchange Commission (SEC) 2a-7 rules.

Modify language to reflect changes to updated Investment Procedures.

- ***Section 7.0 Authorized Financial Dealers and Institutions*** – Added language that the City's Investment Officials will periodically review the approved list of Financial Institutions and broker/dealers to determine the need to add or delete firms and/or individuals from the approved list. The City's Investment Advisor is currently drafting a detailed questionnaire and rating scale for the addition of new broker/dealers to the City's approved list.

- ***Section 5.0 Delegation of Authority (subsection E)*** - Recommended deletion of requirement for Monthly Reports. As noted during the 2010-11 budget process, this recommendation is based on the operational impact on the Finance Department's Investment Unit due to the elimination of staff positions in the Investment Program as approved by the City Council as a budget balancing action. Staff believes Quarterly Reports are comprehensive and suitable for Council oversight and are consistent with reporting requirements in the California Government Code. It is important to note that Monthly Reports are generated for the benefit of external parties and their removal does not reflect a reduction of internal control procedures within the Investment Program. The Investment Program will continue to utilize its daily internal reporting structure.

- ***Section 14.2.b Restructuring Transactions*** - Recommended requiring the Finance Director's prior written approval for restructuring transactions and reporting any executed restructurings to the City Manager within 72 hours and reporting in the Quarterly Investment Reports. This will provide for practical operational efficiencies and implement appropriate notification criteria to the City Manager, City Council, and the Public.

Material Policy Changes -- Recommendations

Add New Asset Classes or Modify Language to Increase Portfolio Diversification Potential.

- ***Section 8.0 Authorized Investments (subsection 4) - Time Deposits*** Added language that deposits are not limited solely to banks and savings and loans with offices located in the San José area. This change allows Investment Officials to improve opportunities for portfolio diversification in the event time deposits outside of the City provide better credit and investment opportunities.

- ***Section 8.0 Authorized Investments (subsection 12) - Municipal Bonds*** – Expanded Investment Policy to allow for the purchase of bonds issued by any of the other 49 states, 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. Currently, the Investment Policy only authorizes the purchase of bonds issued by the City or an agency of the City or the State of California. However, California is currently one of the lowest rated states in the nation and the addition of bonds issued by any of the other 49 states allows Investment officials greater diversity and credit quality in the event Municipal securities are deemed a prudent investment vehicle.

- ***Section 8.0 Authorized Investments (subsection 12) - Municipal Bonds*** Added language allowing the City to consider the mandatory put date or the tender option date rather than the scheduled maturity date, as the final maturity date for Variable Rate Demand Obligations or other securities that include mandatory put provisions or tender option dates. For example, if the City or an agency of the City issues variable rate debt which matures in 30 years but has a "weekly put" provision whereby the bond can be "put" back to the remarketing agent for purchase, then the maturity date is based on the "weekly put" and not the maturity date of 30 years.

- ***Section 8.0 Authorized Investments (subsection 15 & 16) - Mortgage & Asset Backed Securities*** - Added language allowing investment, with certain criteria and restrictions, in securities to improve opportunities for portfolio diversification. These securities are permitted investments under the California Government Code and, at times, offer compelling returns versus alternatives with similar risk characteristics.

Change Current Percent Limitations to Decrease Concentration Risk, Improve Overall Portfolio Credit Profile and Increase Portfolio Diversification Potential.

- ***Section 8.0 Authorized Investments (subsection 18) - Overall Policy Limits*** -- Added language that no more than 10% of the City's portfolio may be invested, in the aggregate, in any single institution. This proposed change will help ensure that concentration risk is mitigated throughout the overall portfolio. For example the Investment Program could currently have a 5% single issuer allocation to Commercial Paper, Bankers Acceptances, Corporate Notes, and Negotiable Certificates of Deposit exposing the portfolio to a 20% concentration in a single issuer. Currently the Investment Policy only places issuer limitations per asset class which leaves the City vulnerable to concentration risk.

- ***Section 8.0 Authorized Investments (subsection 4) - Bankers' Acceptances*** -- Recommend lowering the limit of the percentage of Bankers' Acceptances in the overall portfolio from 25% to 20%.

- ***Section 8.0 Authorized Investments (subsection 6) – Negotiable Certificates of Deposit*** - Recommend lowering the limit of the percentage of Negotiated Certificates of Deposit in the overall portfolio from 25% to 20%.

- ***Section 8.0 Authorized Investments (subsection 8) – Corporate Notes*** Recommend increasing the limit of the percentage of Corporate Notes in the overall portfolio from 15% to 20% (California Code 30%). The proposed_language above

(Section 8.0 subsection 18) that reduces single issuer corporate credit concentration risk allows for increasing diversification potential in this asset class.

- ***Section 8.0 Authorized Investments (subsection 10) - Money Market Mutual Funds*** -- Recommend increasing the limits per individual mutual fund to 10% from 5% and increasing the limits in total overall portfolio to 20% from 15%. This recommendation allows the City to increase the overall credit profile of the portfolio because the City's credit risk is to the underlying assets owned by the mutual fund, versus the entity operating the fund like other asset classes recommended for percentage reductions.

EVALUATION AND FOLLOW-UP

Following direction from the Public Safety Finance and Strategic Support Committee, staff will finalize the amendments to the Investment Policy and the City Attorney's Office will prepare the resolution for City Council approval.

PUBLIC OUTREACH

Not Applicable

COORDINATION

This memorandum was coordinated with the City Attorney's Office and the proposed changes were reviewed with the City Auditor's Office.

COST IMPLICATIONS

Not applicable.

CEQA

Not a Project, File No. PP10-068 (b), Municipal Code or Policy revision.

Scott P. Johnson

SCOTT P. JOHNSON
Director, Finance Department

For questions, please contact Arn Andrews, Division Manager, Finance - Treasury at (408) 535-7041.

City of San José, California

COUNCIL POLICY

TITLE CITY OF SAN JOSE INVESTMENT POLICY	PAGE 1 of 26	POLICY NUMBER 1-12
EFFECTIVE DATE November 3, 1987	REVISED DATE December 8, 2009	

APPROVED BY COUNCIL ACTION 11/03/87, Item 7e(6); 9/20/88, Item 10a, Res. No. 60898; 12/13/88, Item 6f(1), Res. No. 61089; 9/12/89, Item 6f(2), Res. No. 61661; 12/8/92, Item 7e(9); 10/12/93, Item 9f, Res. No. 64925; 1/25/94, Item 7d(4); 2/1/94, Item 6f(8); 3/7/95, Item 7d(5); 4/23/96, Item 9j, Res. No. 66571; 06/26/01, Item 3.10; 5/21/02, Item 3.4, Res. No. 70976; 6/04/02, Item 3.7, Res. No. 71005; 6/24/08, Item 2.13, Res. No. 74474; 6/09/09, Item 2.6, Res. No. 74941; 12/8/2009, Item 3.8(b), Res. No. 75198;

1.0 POLICY

The purpose of this Investment Policy ("Policy") is to establish overall guidelines for the management and investment of the City of San Jose's ("City") public funds.

It is the policy of the City to invest public funds in a manner to meet the City objectives, in order of priority, safety of invested funds, maintenance of sufficient liquidity to meet cash flow needs; and attainment of ~~maximum yield possible~~a rate of return consistent with the first two objectives, while conforming to the provisions of California Government Code Sections 53600 et seq.[1], the Charter of the City of San Jose, the City of San Jose Municipal Code, and this Policy.

2.0 SCOPE

This Policy applies to all funds, entities and investment activities under the Director of Finance's control as accounted for in the Comprehensive Annual Financial Report, including but not limited to the following unless specifically exempted by statute or ordinance:

- General Fund
- Special Revenue Funds
- Debt Service Funds
- Capital Projects Funds
- Enterprise Funds
- Trust and Agency Funds
- Any new fund created by the City Council unless specifically exempted.

1) The City's Deferred Compensation Plan is excluded because it is managed by a third party administrator under the authority of the City's Deferred Compensation Advisory Committee and invested by individual plan participants. Additionally, the City's Retirement Funds are generally excluded because they are managed by the Retirement Administration under the authority of the Retirement Boards.

[1] Even though the provisions of California Government Code Sections 53600 et. seq. do not necessarily apply to the City as a charter city the City has determined that it is prudent to conform this Investment Policy to State law.

2) Proceeds of debt issuances shall be invested in accordance with the investment objectives of this Policy and in accordance with the permitted investment provisions of their specific bond indentures. The reporting requirements in Section 15 shall not apply to bond proceeds held by trustees. Bond proceeds held in various trust accounts are not subject to percentage restrictions specified in Section 8 of this Policy. If in the opinion of the Director of Finance the matching of bond reserve ~~fund~~funds with the maturity schedule of an individual bond issue is prudent, the Director of Finance is authorized to cause the bond reserve fund to be invested in an investment vehicle that is authorized by this Policy but that has a maturity that exceeds the five year limitation specified in Section 12 of this Policy.

3.0 PRUDENCE

"City Investment Officials" means the Director of Finance, Assistant Director of Finance, Division Manager – Treasury, Principal Investment Officer, ~~Investment Officer,~~ Financial Analyst and any other Finance staff that the Director of Finance authorizes in writing. The overall investment program shall be designed and managed with a degree of professionalism worthy of the public trust. City Investment Officials performing duties in furtherance of the investment program, shall act as fiduciaries subject to the Prudent Investor Standard which shall be applied in the context of managing an overall portfolio.

Prudent Investor Standard: Acting with care, prudence and diligence under circumstances then prevailing, 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 of the agency. Individuals charged with responsibility of investing public funds improve their chance of meeting the prudent investor standard by following a strict professional discipline which involves prudence, discretion and intelligence as exercised in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

City Investment Officials, acting in accordance with this Policy and written procedures governing the City's investment program and exercising due diligence, shall be relieved of personal responsibility and liability for an individual security's credit risk or market price changes, provided that deviation from expectations are reported in a timely fashion as required by this Policy and the City's investment program procedures and appropriate action is taken to control adverse developments.

4.0 OBJECTIVES

The primary objectives, in order of priority, of the City's investment program are:

A. Safety: Safety of principal is the foremost objective of the investment program. Investments of the City shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. To attain this objective, the City will diversify its investments by investing funds among a variety of financial institutions and securities offering independent returns. In particular, the City shall seek to preserve principal by mitigating credit risk and market or interest rate risk by doing each of the following:

- Credit risk, defined as the risk of loss due to the failure of the security issuer or backer, will be mitigated by:
    - Limiting investments to ~~the safest types of~~high quality securities;
    - Prequalifying the financial institutions with which the City will do business;
    - Diversifying the investment portfolio so that the failure of any one issuer or backer will not place an undue financial burden on the City; and
    - Monitoring the investment portfolio ~~on a daily basis~~pursuant to Investment Procedures to anticipate and respond appropriately to a significant reduction of credit worthiness of any of the depositories or investment counterparties.

- Market or interest rate risk, defined as the risk that the market value of portfolio securities will fall due to an increase in general interest rates, will be mitigated by:
    - ~~Structuring~~Generally structuring the City's portfolio so that securities mature to meet the City's cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to their maturation to meet those specific needs; and
    - Occasionally restructuring the portfolio to minimize the loss of market value and/or ~~maximize cash flows~~to enhance return/yield subject to the constraints described in Section 14.2 of this Policy.

B. Liquidity: The City's investment portfolio will be structured in a manner which will provide that securities mature at the same time as cash is needed to meet anticipated demands (static liquidity). Additionally, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets (dynamic liquidity). The specific percentage mix of different investment instruments and maturities is described in Section 8.0 of this Policy.

It is the ~~full~~general intent of the City to hold all investments until maturity to ensure the return of all invested principal. However, securities may be sold prior to maturity as needed to comply with the intent of this Policy. While it may occasionally be necessary or strategically prudent for the City to sell a security prior to maturity to either meet unanticipated cash needs, to minimize loss of principal of a security with declining credit, or to restructure the portfolio, this Policy specifically prohibits trading securities for the sole purpose of speculating or taking an unhedged position on the future direction of interest rates. Specifically, "When, as, and if issued" trading and open-ended portfolio restructuring transactions are prohibited; however, purchasing "When, as, and if issued" U.S. Treasuries and U.S. Government Agencies with forward settlement dates not greater than 21 days are permitted. Purchasing "when, as, and if issued" U.S. Treasuries and U.S. Government Agencies with forward settlement dates greater than 21 days are permitted with prior written approval by the Director of Finance.

C. Yield: The City's investment portfolio shall be designed with the objective of attaining a ~~market~~ rate of return throughout budgetary and economic cycles, taking into consideration the investment risk constraints and liquidity needs. Yield on the City's investment portfolio is of secondary importance compared to the safety and liquidity objectives described above. Investments are limited to relatively low-risk securities in anticipation of earning a ~~fair~~rate of return relative to the risk being assumed. Nevertheless, investment performance shall be

~~continually~~periodically monitored and evaluated by the Director of Finance by comparison with other benchmark yields.

5.0 DELEGATION OF AUTHORITY

Authority to manage the City's investment program is derived as follows:

A. Responsibilities of the Finance Department

The Finance Department is charged by the City Charter with responsibility for maintaining custody of all public funds and securities belonging to or under the control of the City, and for the deposit and investment of those funds in accordance with principles of sound treasury management and in accordance with applicable laws and ordinances.

B. Responsibilities of the Director of Finance

The Director of Finance is appointed by the City Manager and is subject to his or her direction and supervision. In accordance with the City Charter, Article VIII, Section 806, the Director of Finance is charged with responsibility for the conduct of all Finance Department functions, including the custody and investment of City funds, and the development of procedures to implement this Policy. The Director of Finance is further responsible for the duties and powers imposed by the general laws of the State of California upon City Treasurers, City Assessors and City Tax Collectors.

Subject to the limitations and requirements specified in this Policy, the Director of Finance and his/her authorized designee(s) can execute agreements and other forms of documentation in order to make investments in Permitted Investments (as defined in Section 8, below). Under the oversight of the Director of Finance, responsibility for the operation of the investment program may be delegated to the Finance staff, who shall act in accordance with established written procedures and internal controls consistent with the Policy. The Director of Finance shall be responsible for all transactions undertaken and shall establish a system of controls in accordance with Section 13.0 of this Policy.

C. Responsibilities of the City Manager

The City Manager is responsible for directing and supervising the Director of Finance. He or she is responsible further to keep the City Council fully advised as to the financial condition of the City.

D. Responsibilities of the City Auditor

The City Auditor is charged by the City Charter with conducting performance audits as assigned by the City Council. A review of the City's investment program could be a part of the responsibility described above.

E. Responsibilities of the City Council

The City Council shall annually review and shall adopt by resolution the Investment Policy as described in Section 17.0. As provided in Section 15.0, the Council shall receive and review ~~monthly and quarterly investment reports.~~Quarterly Investment Reports. The distribution of these ~~monthly and quarterly reports~~Quarterly Reports shall be by electronic means as described in that Section. No less than semi-annually, with the Second Quarterly Report (July – December) and the Fourth Quarterly Report (January – June) the City Council Committee assigned the responsibility for review of Finance Department reports shall have agendized a presentation and overview of the City's Investment Program.

5.1 INVESTMENT PROCEDURES

The Director of Finance shall establish written investment policy procedures for the operation of the investment program consistent with this Policy. Such procedures shall include explicit delegation of authority to persons responsible for investment transactions. No City Investment Official may engage in an investment transaction on behalf of the City except as provided under the terms of this Policy and the written procedures established by the Director of Finance.

6.0 ETHICS AND CONFLICTS OF INTEREST

City Investment Officials involved in the investment process shall refrain from personal business activity that could conflict with proper execution of investments subject to this Policy. City Investment Officials shall avoid all conflicts of interest or appearance of conflicts of interest when performing duties in furtherance of this investment program. The Director of Finance shall immediately disclose any financial interest which is subject to disclosure under the California Political Reform Act or would constitute a conflict of interest under Government Code Section 1090 to the City Manager and the City Attorney. All other City Investment Officials shall immediately disclose any financial interest which is subject to disclosure under the California Political Reform Act or would constitute a conflict of interest under Government Code Section 1090 to the Director of Finance, who in turn will immediately notify the City Manager and the City Attorney. Additionally, City Investment Officials shall comply with the City's Code of Ethics, conflict of interest requirements under state law and the disclosure requirements of the Political Reform Act.

7.0 AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS

A. Standards for Financial Institutions eligible to transact investment business with the City include (collectively, "Financial Institutions"):

- Primary government dealers as designated by the Federal Reserve Bank of New York (Exhibit A), or
- ~~Broker/dealer licensed by the State of California~~
- ~~Member of National Association of Security Dealers~~
- National or state chartered banks, or
- Regional broker/dealers, or
- Direct issuers of securities eligible for purchase by the City
- All must be licensed by the State of California
- All must be members of Financial Industry Regulatory Authority (FINRA)

B. The Director of Finance will maintain a list of ~~f~~Financial ~~i~~Institutions authorized to provide investment services and a list of approved security broker/dealers after a careful review of their qualifications and creditworthiness. All financial institutions and broker/dealers who desire to do business with the City shall provide the necessary information (e.g. audited financial statements, proof of state registration, proof of ~~National Association of Security Dealers~~FINRA certification, etc.) from which the City can determine their creditworthiness, the existence of any pending legal action against the firm or the individual broker/~~dealer~~s who work directly with the City, as well as an understanding of the security markets that they serve.

The Director of Finance will conduct an annual review of the financial condition and registrations of ~~qualified~~ approved F~~f~~inancial I~~i~~nstitutions and security broker/dealers. Audited financial statements, collected as part of the annual review will be on file (either paper or electronic) for each F~~f~~inancial I~~i~~nstitution and broker/dealer with which the City invests. City Investment Officials will periodically review the approved list of Financial Institutions and security broker/dealers to determine the need to add to or delete from the approved list.

The Director of Finance will make a determination on whether an Agreement (consultant or service agreement) needs to be executed with the financial institution based on the scope of services and compensation provided. For example, City currently executes an Agreement for Investment Custodial Services ~~and~~as well as Investment Advisory Services. While it is not currently being contemplated, to the extent any broker/dealer is providing investment advisory services, as opposed to traditional brokerage services, the City will enter into an Agreement for those services. Additionally, any firm in which the City enters into a Repurchase Agreement must meet the requirements outlined in Section 8.0(7) of the Policy. The City requires that an agreement for services be executed prior to entrusting its funds to any dealer or F~~f~~inancial I~~i~~nstitution, and that up-to-date financial statements be sent to the Director of Finance upon their issuance.

C. After the annual Council adoption of the Policy, the Director of Finance shall send a copy of the current edition of the Policy to all Financial Institutions and broker/dealers, which are approved to execute investment transactions with the City. Confirmation of receipt of this policy shall be considered evidence that the Financial Institution and broker/dealer understands the City's Policy and intends to sell the City only appropriate investments authorized by this Policy.

8.0 AUTHORIZED INVESTMENTS

All investments shall conform to Sections 53600 et seq. of the California Government Code and as described within the Policy ("Permitted Investments"). Where this section specifies a percentage limitation for a particular category of investment, that percentage is applicable only at the date of purchase. If subsequent to purchase, portfolio percentage constraints are above the maximum thresholds due to changes in value of the portfolio, or changes due to revisions of the Policy, then the affected securities may be held to maturity in order to avoid potential principal losses. However, the Director of Finance may choose to rebalance the portfolio (pursuant to Section 14.2 of the Policy) if percentage imbalances are deemed to impair portfolio diversification.

If subsequent to purchase, securities are downgraded below the minimum acceptable ratings level (below prime for short term ratings, or below investment grade for long term ratings), then the securities shall be reviewed for possible sale within a reasonable amount of time after the downgrade. In either instance listed above, the fact will be disclosed in the ~~monthly or quarterly investment report~~Quarterly Investment Report as described in Section 15.0 of this Policy.

Permitted Investments and applicable limitations shall include:

1) United States Treasury Obligations, including Bonds, Notes and Bills:
   - There is no maximum portfolio limit.
   - Purchase in Treasury securities shall not exceed five years to maturity.

2) United States Government Agency Issues
   - The purchase of United States Federal Government Agency securities will be limited to the senior, non-subordinated issues of the Federal Farm Credit Banks (FFCBs), the Federal Home Loan Banks (FHLBs), Federal Home Loan Mortgage Corporation (FHLMC), and the Federal National Mortgage Association (FNMA~~) and the Student Loan Marketing Association (SLMA~~). This limitation shall not apply to money market mutual funds described in Subsection 10.
   - There is no maximum portfolio limit.
   - Purchase in eligible Agency securities shall not exceed five years to maturity.
   - The purchase of subordinated debt of a United States Government Agency will be classified as Corporate Note as listed in this Policy, and as such subject to limitations of that security type.

3) Bankers Acceptances (BAs)
   - BAs eligible for investment must be rated "P1, A1, or F1" or better by two of the three nationally recognized rating services, Moody's, S&P, or Fitch, respectively. No rating may be lower than any of the ratings listed above.
   - The purchase is limited to BAs issued by domestic U.S. or foreign banks and which must be rated by Fitch ~~Financial Services Inc. ("Fitch")~~ as follows: an issuer rating of "B" or better for domestic U.S., "C" or better for California banks, or "A/B" or better for foreign banks, or if the issuing bank issues debt, other than BAs, the outstanding debt must be rated "A3, A-, or A-" or higher, respectively by Moody's, S&P or Fitch. No rating may be lower than any of the ratings listed in the preceding sentence.
   - Foreign BAs must be dollar-denominated.
   - No more than 5% of the portfolio shall be invested in any single institution.
   - No more than ~~25~~20% of the portfolio shall be invested in BAs.
   - The maturity of any BA shall not exceed 180 days.

4) Time Deposits
   - Deposits up to the federally insured (FDIC) limit ~~and are~~may be invested in, but are not limited to banks and savings and loans with offices located in the San Jose area.
     - No more than $10 million of the portfolio shall be invested in federally insured time deposits of which no more than 5% shall be invested in one issuer.
     - Deposits shall not exceed the net worth of the bank or savings and loan.
     - The maturity of such deposits shall not exceed three years.
   - Deposits over the federally insured limit (FDIC) ~~are~~may be invested in, but are not limited to banks and savings and loans in the San Jose area.
     - Depositories must have an issuer rating of "B" or better by Fitch.
     - Deposits shall be collateralized in the manner prescribed by State law for depositories.
     - No more than $10 million of the portfolio shall be invested in non-negotiable and collateralized deposits of which no more than 5% shall be invested in one issuer.
     - Deposits shall not exceed the net worth of the bank or savings and loan.
     - The maturity of non-negotiable and collateralized deposits shall not exceed 18 months.

5) Commercial Paper (CP)

- ~~The California Government Code restricts cities to investing in commercial paper of prime quality of the highest rankings or of the highest letter and number rating as provided for by Moody's Investment Service (Moody's), Standard and Poor's (S&P) or Fitch.~~
- Commercial paper eligible for investment must be rated "P1, A1, or F1" or better by two of the three nationally recognized rating services, Moody's, S&P, or Fitch, respectively. No rating may be lower than any of the ratings listed above.
- Issuing corporations must be organized and operating within the United States and have total assets in excess of $500,000,000 and shall issue debt, other than commercial paper, if any, that is rated "A3, A-, or A-" or higher, respectively by Moody's, S&P or Fitch. No rating may be lower than any of the ratings listed in the preceding sentence.
- Purchase of commercial paper may not represent more than 10% of an issuing corporation's commercial paper.
- No more than 5% of the portfolio shall be invested in any single institution.
- No more than 20% of the portfolio shall be invested in commercial paper.
- The maturity of the commercial paper shall not exceed 270 days.

6) Negotiable Certificates of Deposit (NCDs)

- Depositories shall be limited to banks and savings and loans with an issuer rating of "A/B" or better by Fitch.
- No more than the lesser of the net worth of the institution or 5% of the portfolio shall be invested in any single institution.
- No more than ~~25~~20% of the portfolio shall be invested in NCDs.
- The maturity of the NCDs shall not exceed 180 days.

7) Repurchase Agreements (Repos)

- Repos are executed only with primary dealers of the Federal Reserve Bank of New York ~~and financial institutions~~ which have entered into the City's Master Repurchase Agreement and any subsequent amendments to the Master Repurchase Agreement.
- Securities accepted as collateral for repurchase agreements are U.S. Treasury or U.S. Federal Government Agency issues permitted by this Policy and the limitations set for under Section 8.0(1) and 8.0(2).
- The full market value of securities (including accrued interest) accepted as collateral as authorized by this Policy shall be at the time of transfer equal to at least 102 percent of the face value of the Repo.
- For other than overnight investments, the securities transferred shall be marked to market on a daily basis and maintained at a market value equal to at least 102 percent of the repurchase agreement's face value.
- ~~There is no maximum portfolio limit.~~ No more than 50% of the portfolio shall be invested in repos.
- No more than 10% of the portfolio shall be invested in a repo with any single institution.
- The maturity of any Repo shall not exceed ~~10~~92 days.

8) Corporate Notes

- Securities eligible for investment must be rated "A3, A-, or A-" or better by two of the three nationally recognized rating services~~.~~—, Moody's, S&P, or Fitch, respectively. No rating may be lower than any of the ratings listed above.
-
- No more than 5% of the portfolio shall be invested in any single institution.
- Medium-term corporate notes may not exceed ~~15~~20% of the City's portfolio.
- The maturity of any corporate note shall not exceed three years.

9) Local Agency California Investment Fund (LAIF)

- Funds may be invested in LAIF; a State of California managed investment pool, up to the maximum dollar amounts per separate legal entity in conformance with the account balance limits authorized by the State Treasurer.
- Annual review of LAIF's Pool Money Investment Board Annual Report will be conducted to continue to ensure LAIF's investment policy, standards, and rate of return are compatible with the City's risk tolerance.

10) Money Market Mutual Fund

- An investment objective of the fund must be the maintenance of a price per share of $1.00.
- Fund is registered with the Securities and Exchange Commission (SEC) and complies with the most current guidelines of Rule 2a-7 and other rules under the Investment Company Act of 1940 governing the operation of money market funds.
- Must meet either one of the following credit criteria for investment:
  a. ~~Obtained the highest ranking or highest letter and numerical rating provided by not less than two nationally recognized rating organizations~~The Fund must be rated by not less than two of the following: Moody's -rated Aaa, S&P-rated AAAm, or Fitch-rated AAA. ; or
  b. Retained an investment adviser registered with the SEC, or exempt from the SEC registration requirements with not less than five years experience investing in securities and obligations authorized by the California Government Code 53601 and managing money market mutual funds with assets under management in excess of $500 million.
- The Fund invests only in U.S. Treasury and U.S. Federal Government Agency securities, and in repurchase agreements backed by U.S. Treasury and U.S. Federal Government Agency securities.
- No more than ~~5~~10% of the portfolio shall be invested in any one money market mutual fund.
- No more than ~~15~~20% of the portfolio shall be invested in money market mutual funds.

11) Reverse Repurchase Agreements (Reverse Repos)

- Except as otherwise authorized by the City Council, the use of reverse repurchase agreements will be limited to those occasions where unanticipated, short-term cash requirements can be met more advantageously by initiating a reverse repurchase agreement than by selling a security into the secondary market prior to its maturity.
- Reverse repurchase agreements are executed only with primary dealers of the Federal Reserve Bank of New York which have signed the City's Master Repurchase Agreement and any subsequent amendments to the Master Repurchase Agreement.
- Under no circumstances shall the City sell securities through reverse repurchase agreements for the purpose of financing the acquisition of other securities.

- The term of any reverse repurchase agreement shall be limited to 30 days.
- The amount of the agreement may not exceed the lesser of $25 million or 20% of the base value of the portfolio, and only a single agreement shall be in effect at one time.
- Prior written approval by the City Manager or his or her designee is required to enter into a reverse repurchase agreement, and the fact that such a reverse repurchase agreement has been executed will be reported in writing within 72 hours to the City Manager, City Council and City Auditor and will also be included in the ~~Monthly~~Quarterly Investment Report.

12) ~~California~~ Municipal Bonds

- ~~California municipal~~Municipal bonds are debt obligations issued by the ~~State of California~~ state and local governments and their agencies ~~within the State of California including~~ such as cities, counties, government retirement plans, school districts, state universities, sewer districts, municipally owned utilities and authorities operating bridges, airport and other transportation facilities; including bonds payable solely out of the revenue from a revenue-producing property owned, controlled, or operated by a state or local agency. No more than 20% of the total portfolio shall be invested in ~~California~~ municipal bonds. ~~California municipal bond categories are~~Municipal bonds are further classified as follows:

  - Category 1 - Bonds issued by the City or agency[2] of the City
    - Securities eligible for investment must be rated ~~AA~~, A3, A-, A- or better by two of the three nationally recognized credit rating organizations ~~(~~, Moody's, Standard & Poor's or Fitch~~)~~, respectively; or if deemed appropriate for purchase by the Director of Finance if the issuing agency does not apply for a rating. No rating may be lower than any of the ratings listed above. Such ~~rating~~ratings must be the issuing agency's underlying rating, irrespective of any credit enhancements obtained from third party organizations.
    - No more than 5% of the total portfolio for each separate legal entity with an aggregate limit in bonds issued by the City or its agencies not to exceed ~~15~~10% of the total portfolio.
    - The maturity shall not exceed five years unless there is a mandatory put provision or tender option date imbedded into the security; then the date of the put provision shall be used to determine the maturity.
    - Maturity may exceed five years without a mandatory put provision or tender option date imbedded into the security when prior approval is obtained in writing from the Director of Finance and the City Manager.
    - Maturities exceeding five years will be specifically delineated in the Quarterly Investment Report.

  - Category 2 - Bonds issued by the State of California
    - Obligations must be rated in the ~~AA~~A3, A-, A- or better category by two of the three nationally recognized credit rating organizations ~~(~~, Moody's, Standard &

[2] *"Agency of the City"* includes all "component units" of the City of San José as defined in the City's Comprehensive Annual Financial Report (CAFR) in accordance with generally accepted accounting principles, including, but is not limited to, the Redevelopment Agency of the City of San José ("Redevelopment Agency"), the City of San José Financing Authority, the San José – Santa Clara Clean Water Financing Authority, the City of San José Parking Authority and any other Joint Powers Authority created in which the City and/or the Redevelopment Agency is a majority obligor or participant.

Poor's or Fitch~~).~~, respectively). No rating may be lower than any of the ratings listed above. Such rating must be the issuing agency's underlying rating, irrespective of any credit enhancements obtained from third party organizations.
- No more than 5% of the total portfolio shall be invested in bonds issued by the State of California.
- The maturity, mandatory put provision, or tender option date shall not exceed five years.

- Category 3 - Bonds issued by any other local agency within the State of California
  - Obligations must be rated in the ~~AA~~A3,A-, A- or better category by two of the three nationally recognized credit rating organizations ~~(~~, Moody's, Standard & Poor's or Fitch~~) or~~, respectively. No rating may be lower than any of the ratings listed above. Such ratings must be ~~rated AAA through~~the issuing agency's underlying rating, irrespective of any credit enhancements ~~the issuing agency has~~ obtained from third party organizations.

  - ~~No more than 10% of the total portfolio shall be invested in bonds of other local agencies.~~
  - Investments in this category may not represent more than 10% of the issuing entity's outstanding debt.
  - The maturity, mandatory put provision, or tender option date shall not exceed five years.
  - No more than 5% of the total portfolio shall be invested in any one issuer.

- Category 4 - Bonds issued by any of the other 49 states, 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 United States, in addition to California.
  - Obligations must be rated in the A3, A-, A- or better category by two of the three nationally recognized credit rating organizations, Moody's, Standard & Poor's or Fitch, respectively. No rating may be lower than any of the ratings listed above. Such ratings must be the issuing agency's underlying rating, irrespective of any credit enhancements obtained from third party organizations.
  - The maturity, mandatory put provision, or tender option date shall not exceed five years.
  - Investments in this category may not represent more than 10% of the issuing entity's outstanding debt.
  - Investments in this category may not represent more than 10% of the issuing entity's outstanding debt.
  - No more than 5% of the total portfolio shall be invested in any one issuer.

13) Investment Agreements (IA):

An IA is a contract providing for the lending of issuer funds to a financial institution (the "Provider") which agrees to repay the funds with interest under predetermined specifications. IAs may be used for the investment of bond proceeds in accordance with the permitted investment provisions of the specific bond indentures. To reduce the risk associated with a Provider's inability to meet its contractual obligations, the following safeguards are required in the use of an IA:

- Competitive bidding of the investment agreement pursuant to the Internal Revenue Code and any regulations promulgated thereto;
- Provider (or guarantor of Provider) rated AA or above from at least one national rating agency and ratings in the "AA" category from at least one other national rating agency;
- Provider's participation in the financing will not adversely affect the transaction, including the expected rating on the Bonds;
- Provider downgrade provisions in order to (i) allow the City to terminate the Agreement and withdraw the par value (outstanding principal balance and accrued interest) of the invested proceeds with no penalty or (ii) to require the Provider to increase the collateral level;
- Collateralization of at least 104~~%;~~% (including accrued interest);
- The collateralization requirement does not apply to Conduit Financings;
- Collateral held by a third party;
- ~~Only top rated securities be used as collateral (U.S. Treasuries or Agencies);~~
- Securities accepted as collateral for repurchase agreements are U.S. Treasury or U.S. Federal Government Agency issues permitted by this Policy and including the limitations set for under Section 8.0(1) and 8.0(2) of this Policy. In addition, with the prior written approval of the Director of Finance, securities listed in Section 8.0(15) will be accepted as collateral.
- Agreement to include termination provisions in the event of Provider breach or Provider downgrade; and
- Trustee to monitor the Provider's rating, securities, and collateral value on a weekly basis.

14) Stocks: ~~Any~~From time to time stock may be received as a gift, through bankruptcies or as payment in lieu of monies due the City. Such stock shall be sold ~~immediately upon receipt,~~ unless received through a gift or bequest with restrictions on its sale. Sale proceeds will be distributed to the appropriate program fund. If the stock has no market value or if the cost of selling it exceeds the market value, the stock will be written off or monitored periodically to be sold when a break-even market value can be realized.

15) Mortgage Backed Securities (MBS) and Collateralized Mortgage Obligations (CMO)

- Must be issued by a United States Government Agency.
- Must be AAA rated or its equivalent or better by a nationally recognized rating service. If rated by any of the three rating agencies, the ratings may not be lower than those listed above by any of the rating agencies.
- The maturity of any MBS or CMO security shall not exceed 5 years except with prior written approval from the Director of Finance.
- Maturities exceeding five years will be specifically delineated in the Quarterly Investment Report.
- No more than 10% of the portfolio shall be invested in MBS and CMO in aggregate

16) Asset Backed Securities (ABS)

- Must be AAA rated or its equivalent or better by a nationally recognized rating service. If rated by any of the three rating agencies, the ratings may not be lower than those listed above by any of the rating agencies.

- The maturity of any ABS security shall not exceed 5 years.
- The issuer of the ABS security must have an A3, A-, or A- rating or better by Moody's, S&P, or Fitch, respectively, of its underlying debt. If rated by any of the three rating agencies, the ratings may not be lower than those listed above by any of the rating agencies.
- The ABS security shall only be backed by commercial and consumer receivables.
- No more than 5% of the portfolio shall be invested in ABS.

17) Ineligible Investments

- Ineligible investments include common stock (with the exception noted above in Section 8.14), inverse floaters, range notes, mortgage-derived interest-only strips, or any security that could result in zero interest accrual if held to maturity and any investments not authorized by this Policy unless otherwise approved by the City Council.

18) Combined Issuer/Institution Limits: No more than 10% of the portfolio shall be invested in aggregate of any single institution of the following types: Bankers Acceptances, Commercial Paper, Negotiable Certificates of Deposits, and Corporate Notes.

9.0 COLLATERALIZATION

Collateralization is required on two types of investments: non-negotiable and collateralized time deposits and repurchase agreements.

1) Non-negotiable and collateralized time deposits with banks and savings and loans
   - Shall be collateralized in the manner prescribed by California Government Code 53652 for depositories accepting municipal investment funds.

2) Repurchase Agreements
   - The types of securities to be accepted as transferred securities in repurchase agreements in which the City is the buyer shall be limited to U.S. Treasury or U.S. Federal Government Agency issues permitted under this Policy. The City shall maintain a preference for collateral of shorter-term maturities.
   - The full market value (including accrued interest) of the securities used as collateral for the repurchase agreements shall not be allowed to fall below 102% of the value of the repurchase agreement as provided in the Master Repurchase Agreement.
   - Substitutions of transferred securities shall be limited to U.S. Treasury ~~Bills~~Securities permitted under this Policy and may not be made without prior written approval by the ~~City~~ Director of Finance.

10.0 SAFEKEEPING AND CUSTODY

All securities owned by the City shall be held in safekeeping by the City's custodial bank or by a third party bank trust department, acting as agent for the City under the terms of a custody agreement or master repurchase agreement. All security transactions, including collateral for repurchase agreements, entered into by the City shall be conducted on a delivery-versus-payment

(DVP) basis through the City's safekeeping agent. Securities held in custody for the City shall be independently audited on an annual basis to verify investment holdings.

11.0 DIVERSIFICATION

The City, consistent with the primary objectives of safety, liquidity and yield, will diversify its investment by security type, issuer and maturity dates. Portfolio percentage and/or dollar limits are indicated in Section 8.0 of this Policy.

12.0 MAXIMUM MATURITIES

The City's investment portfolio shall be structured to provide that sufficient funds from investments are available to meet the City's anticipated cash needs. The choice of investment instruments and maturities shall be based upon an analysis of anticipated cash needs, existing and anticipated revenues, interest rate trends and specific market opportunities. The average weighted maturity of the investment portfolio will not exceed two years, and no investment will have a maturity of more than five years from its date of purchase unless specifically approved according to the provisions set forth elsewhere in this Policy.

~~Bond reserve funds established by the issuance of bonds may be invested in securities exceeding five years if the maturities of such investments are made to coincide with the expected use of the funds.~~

13.0 INTERNAL CONTROLS

The Director of Finance is responsible for establishing and maintaining an internal control structure designed to ensure that the City's assets are protected from loss, theft or misuse. The internal control structure shall be designed to provide reasonable assurance that those objectives are met. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits to be derived and that the valuation of costs and benefits requires estimates and judgments by management. Internal control procedures shall address:

- Separation of duties
- Control of collusion
- Custodial safekeeping
- Avoidance of physical delivery of securities
- Written confirmation of transfers for investments and wire transfers
- Written procedures for placing investment transactions
- Delegation of authority to investment officials

14.0 PERFORMANCE STANDARDS

The investment portfolio shall be designed with the overall objective of safety, liquidity and a rate of return on investment commensurate with the investment risk constraints and the cash flow needs.

14.1 MARKET YIELD (BENCHMARK)

The City's investment portfolio is ~~primarily~~generally managed on a "buy and hold" strategy. Given this strategy, the basis used by the Director of Finance to determine whether market yields are being achieved shall be to identify a benchmark comparable to the weighted average maturity and average composition of the investment portfolio, which varies over time. The benchmark used shall be delineated in the Quarterly Investment Report and may be modified due to material changes in the portfolio's composition or weighted average maturity. If the benchmark is changed, the modification shall be explained in the Quarterly Investment Report.

The City's Investment Portfolio shall be designed with the objective of attaining a ~~market~~ rate of return throughout budgetary and economic cycles, taking into consideration the investment risk tolerance and liquidity needs of the City. Yield on the City's investment portfolio is of secondary importance to the safety and liquidity objectives described in Section 4.0 of the Policy.

14.2 RESTRUCTURING TRANSACTIONS

a) General Definitions

The restructuring process involves a change in the composition of the portfolio such that the aggregate portfolio after all transactions are executed meets original goals and constraints of the Policy and performance has been improved. Restructuring opportunities are not a function of time but rather a result of changing market conditions. Conditions that are generally favorable to restructurings are:

- availability of more ~~efficient~~beneficial issues,
- changes in the shape of the yield curve,
- changes in quality or sector spreads.

A restructured portfolio must continue to generate sufficient cash flow to meet the City's cash requirements without impairing the overall quality/diversification constraints of the portfolio.

b) Specific Requirements

- Restructuring transactions in the City's portfolio shall not exceed $40 million (par value) per month in original securities exchanged for replacement securities.
- Prior conceptual approval shall be obtained in writing from the ~~City Manager and the~~ Director of Finance.
- Executed restructuring transactions will be reported to the City Manager within 72 hours.

- Executed restructuring transactions will be included in the ~~Monthly~~Quarterly Investment Report.
- Net sales gains or losses shall not be incurred to the point of radically altering the current month's earned interest yield (plus or minus 30 basis points).

15.0 REPORTING AND DISTRIBUTION

The Director of Finance shall prepare and submit ~~monthly and~~ Quarterly Investment Reports containing the information described in Sections 15.1 ~~and 15.2~~ to be posted to the City's internet site for public access and distribute a hard copy of the reports to the City Clerk's Office for public review. ~~In addition, the Director of Finance shall distribute these reports through electronic means to the City Council, the City Manager, and the City Auditor. In the event of any unforeseen technological issues which prevent an electronic posting and/or distribution, the Director of Finance shall distribute a hard copy report in a reasonable time after which such report is generated by the Finance Department.~~ In the event there are exceptions to the Policy, the Director must report as described in Section 15.~~3~~2.

15.1 QUARTERLY INVESTMENT REPORTS

The ~~quarterly reports~~Quarterly Investment Reports shall be placed on the next available agenda of the City Council Committee responsible for the review of Finance Department items after the electronic distribution and posting of the reports. At least semi-annually, the Committee shall receive an oral presentation on the contents of the Quarterly Investment Report as described in Section 5.E. The ~~quarterly investment report~~Quarterly Investment Report will include the following information portfolio statistics, portfolio performance, compliance reporting requirements, investment trading activity and investment strategy:

- Portfolio Statistics
  - Classification of the investment, the percentage of the total portfolio which each type of investment represents, issuer, CUSIP, purchase date, rating of security, date of maturity, par and dollar amount invested on all securities and investments
  - Current market value and the source of the market value
  - Weighted average maturity of the investment portfolio
  - Trend of average portfolio maturity
  - Maturity aging by type of investment
  - Unrealized gain or loss resulting from appreciation or depreciation in the market value of securities
  - Portfolio turnover rate and trend

- Portfolio Performance
  - Weighted average yield on reporting quarter's purchases
  - Weighted average yield on reporting quarter's sales and/or maturities
  - Weighted average yield of the portfolio based upon book value as compared to a benchmark
  - Trend of the monthly earned interest yield on investments
  - Trend of the monthly days to maturity and yield

- Compliance Reporting Requirements
  - Cash management projection: Statement denoting the ability of the City to meet its expected obligations over the next six months
  - Statement of compliance with the Policy: Reasons for and number of violations or exceptions to the investment policy during the quarter being reported on, as well as prior violations or exceptions which have not yet been corrected
  - Comparison of budgeted investment earnings to actual earnings for the reporting quarter and fiscal year-to-date
  - Distribution reports by bank and broker/dealer

- Investment Trading Activity
  - All investment transactions occurring during the quarter whether or not the transaction has been fully settled
  - Separation of realized trading gains or losses from interest received on trading activity (Since the City is not involved in active trading, this will occur only when a security must be sold prior to maturity as defined in Section 4.0.B.)
  - Aggregate commitments to purchase securities or make other payments to dealers in a manner to permit adequate cash need forecasting
  - A brief description of executed reverse repos and the associated interest cost and interest earnings from the transactions
  - A brief description of executed restructuring transactions. Number and dollar volume of trades executed for the sole purpose of restructuring the portfolio and analysis of benefit derived from those trades
  - A description of any security purchased during the quarter with a maturity exceeding five years
  - A description of any security downgraded below the minimum acceptable ratings level (below prime for short term ratings, or below investment grade for long term ratings)

- Investment Strategy
  - Description of the current investment strategy and the assumptions upon which it is based

~~15.2 MONTHLY INVESTMENT REPORTS~~

~~An abbreviated monthly investment report summarizing the highlights of the monthly investment activity will be distributed in accordance with provisions in Section~~
15.~~0. The abbreviated monthly investment report will include the following portfolio statistics, portfolio performance, compliance reporting requirements, and investment strategy.~~

- ~~Portfolio Statistics~~
  - ~~Investments in the City's portfolio as of the end of the month~~
  - ~~Related earnings associated with each investment held during the reporting period~~
  - ~~Purchase activity associated with each investment broker for the reporting period~~
  - ~~Classification of the investment, issuer, date of maturity, par and dollar amount invested on all investments as of the end of the month~~
  - ~~Market value of investments in the City's portfolio as of the end of the month~~

- ~~Portfolio Performance~~
  - ~~Comparison of budgeted investment earnings to actual earnings for the reporting period and fiscal year to date~~
  - ~~Investment portfolio performance measurement~~
  - ~~Trend of the monthly earned interest yield on investments~~

- ~~Compliance Reporting Requirements~~
  - ~~Statement of compliance with the Policy: Reasons for and number of violations or exceptions to the Policy during the month being reported on, as well as prior violations or exceptions which have not yet been corrected. If there has been no violations of or exceptions to the Policy during the reporting period, a statement to that effect shall be set forth in the report.~~

- ~~Investment Strategy~~
  - ~~Description of the current investment strategy and the assumptions upon which it is based~~

~~15.3~~2 REPORTING POLICY EXCEPTIONS

While this Policy prescribes various maximums, minimums and other relatively arbitrary numerical limits, it is intended primarily to be a management tool. When the Director of Finance determines that an exception to one of the Policy's numerical limits is in the best interest of the City, and is otherwise consistent with the Policy, such exception is permitted so long as it is consistent with applicable City, State and Federal laws. Whenever an exception or violation of this Policy is made, that fact~~,~~ shall be reported to the City Manager within three business days, and to the City Council within ~~one business day~~10 days of its discovery. Major exceptions will be reported immediately. All exceptions to the Policy and the appropriate explanation or justification for the exception shall be included in the ~~Monthly~~Quarterly Investment Report. ~~Sudden large fluctuations~~Fluctuations in portfolio assets can cause technical exceptions to the various percentage limits of the Policy which should not be interpreted as "reportable exceptions". ~~Provided that the portfolio make-up can be readjusted to Policy limits within one working day of a significant increase or decrease in portfolio assets, such temporary percentage exceptions need not be reported as violations or exceptions to this Policy.~~The Director of Finance may choose to rebalance the portfolio if percentage imbalances are deemed to impair portfolio diversification.

15.4 15.3 SEMI-ANNUAL COMPLIANCE AUDITS

No less than semi-annually each year, a compliance audit shall be conducted of the City's investment program to determine whether the City's investments within the City's pooled portfolio are in compliance with the City's Investment Policy, internal controls, and department procedures. If the City Council does not direct that the compliance audits be included in the City Auditor's annual workplan, then the Director of Finance shall cause such compliance audits to be conducted by an external auditor.

16.0 SOCIAL RESPONSIBILITY – FORECLOSURE MITIGATION

In addition to and subordinate to the objectives set forth in Section 4.0 herein, investment of funds should be guided by the following socially responsible investment goals when investing in permitted short-term investment instruments provided by mortgage servicers. To the extent competing financial institutions offer short-term investment instruments of substantially equivalent safety, liquidity and yield, the level of participation in the federal Home Affordable Modification Program (HAMP) and/or a Community Reinvestment Act rating of "satisfactory" or higher will be used as an investment criteria to differentiate between similar financial institutions' short-term investment instruments.

17.0 INVESTMENT POLICY REVIEW/ADOPTION

The Policy shall be adopted by resolution of the City Council on an annual basis. This Policy shall be reviewed annually to ensure its consistency with respect to the overall objectives of safety, liquidity and yield, and its relevance to current laws and financial trends. An annual Statement of Investment Policy including ~~any~~ proposed amendments to the Policy with the exception of minor Policy changes shall be prepared by the Director of Finance for the review and recommendation of the City Council Committee assigned the responsibility for review of Finance Department reports prior to submission to the entire City Council for consideration and approval.

18.0 TRAINING AND CONTINUING EDUCATION

The City strives for professionalism and accountability in the investment of its funds. In order to ensure the highest possible professional standards, the City Investment Officials as defined in the Policy, are encouraged to complete at least 16 hours per year of continuing education programs or other training in cash and investment management.

19.0 GLOSSARY

Definitions of investment-related terms are listed on Exhibit B.

EXHIBIT A

LIST OF THE PRIMARY GOVERNMENT SECURITIES DEALERS REPORTING TO THE GOVERNMENT SECURITIES DEALERS STATISTICS UNIT OF THE FEDERAL RESERVE BANK OF NEW YORK

BNP Paribas Securities Corp.
Banc of America Securities LLC
Barclays Capital Inc.
Cantor Fitzgerald & Co.
Citigroup Global Markets Inc.
Credit Suisse Securities (USA) LLC
Daiwa Securities America Inc.
Deutsche Banc Securities Inc.
~~Dresdner Kleinwort Wasserstein Securities LLC~~
Goldman, Sachs & Co.
~~RBS Securities, Inc.~~
HSBC Securities (USA), Inc.
Jefferies & Company, Inc
J. P. Morgan Securities, Inc
Mizuho Securities USA Inc.
Morgan Stanley & Co. Incorporated
Nomura Securities International, Inc.
RBC Capital Markets Corporation
RBS Securities Inc.
UBS Securities LLC

NOTE: This list has been compiled and made available for statistical purposes only and has no significance with respect to other relationships between dealers and the Federal Reserve Bank of New York. Qualification for the reporting list is based on the achievement and maintenance of the standards outlined in the Federal Reserve Bank of New York's memorandum of January 22, 1992.

Government Securities Dealers Statistics Unit
Federal Reserve Bank of New York
~~April 7, 2009~~May 1, 2010

NOTE: The City's Finance Department will replace this list in the official Investment Policy as changes are made by the Federal Reserve Bank of New York.

EXHIBIT B

GLOSSARY

ACCRETION: Adjustment of the difference between the price of a bond bought at an original discount and the par value of the bond.

AGENCIES: Federal agency securities and/or Government-sponsored enterprises (GSEs), also known as U.S. Government instrumentalities. Securities issued by Government National Mortgage Association (GNMA) are considered true agency securities, backed by the full faith and credit of the U.S. Government. GSEs are financial intermediaries established by the federal government to fund loans to certain groups of borrowers, for example homeowners, farmers and students and are privately owned corporations with a public purpose. The most common GSEs are Federal Farm Credit System Banks, Federal Home Loan Banks, Federal Home Loan Mortgage Association, and Federal National Mortgage Association.

AMORTIZATION: Accounting procedure that gradually reduces the cost value of a limited life or intangible asset through periodic charges to income. For fixed assets, the term used is "depreciation". It is common practice to amortize any premium over par value paid in the purchase of preferred stock or bond investments.

APPRECIATION: Increase in the value of an asset such as a stock bond, commodity or real estate.

ASKED PRICE: The price a broker/dealer offers to sell securities.

ASSET BACKED: A type of security that is secured by receivables, such as credit card and auto loans. These securities typically pay principal and interest monthly.

BANKERS' ACCEPTANCE (BA): A draft or bill or exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the issuer. This money market instrument is used to finance international trade.

BASIS POINT: One-hundredth of one percent (i.e., 0.01%).

BENCHMARK: A comparative base for measuring the performance or risk tolerance of the investment portfolio. A benchmark should represent a close correlation to the level of risk and the average duration of the portfolio's investment.

BID PRICE: The price a broker/dealer offers to purchase securities.

BOND: A financial obligation for which the issuers promises to pay the bondholder a specified stream of future cash flows, including periodic interest payments and a principal repayment.

BOOK 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, and includes interest earnings and realized gains and losses on the portfolio.

BOOK VALUE: The value at which a debt security is shown on the holder's balance sheet. Book value is acquisition cost less amortization of premium or accretion of discount.

BROKER: A broker acts as an intermediary between a buyer and seller for a commission and does not trade for his/her own risk and account or inventory.

~~CALIFORNIA MUNICIPAL BONDS: Debt obligations issued by State of California and local governments and their agencies within the State of California including cities, counties, government retirement plans, school districts, state universities, sewer districts, municipally-owned utilities and authorities running bridges, airports and other transportation facilities.~~

CALLABLE SECURITIES: A security that can be redeemed by the issuer before the scheduled maturity date.

CASH FLOW: An analysis of all changes that affect the cash account during a specified period.

CERTIFICATE OF DEPOSIT (CD): A time deposit with a specific maturity evidenced by a certificate. Large-denomination CD's are typically negotiable.

COLLATERAL: Securities, evidence of deposit or other property which a borrower pledges to secure repayment of a loan. Also refers to securities pledged by a bank to secure deposits of public monies.

COLLATERALIZED MORTGAGE OBLIGATION (CMO): A type of mortgage-backed security that creates separate pools of pass-through rates for different classes of bondholders with varying maturities, called tranches. The repayments from the pool of pass-through securities are used to retire the bonds in the order specified by the bonds' prospectus.

COMMERCIAL PAPER: Short-term, unsecured, negotiable promissory notes of corporations.

COMMERCIAL RECEIVABLES: Business debt owed to a creditor which may be used as collateral for asset backed securities. These receivables include equipment leases, building leases, and other business loans.

COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR): The official annual financial report for the City. It includes combined statements and basic financial statements for each individual fund and account group prepared in conformity with Generally Accepted Accounting Principles (GAAP).

CONDUIT FINANCING: A financing in which a governmental agency issues debt and the proceeds of the issue are loaned to a nongovernmental borrower who then applies the proceeds for a project financing or (if permitted by federal tax laws for a qualified 501(c)(3) bond) for working capital purposes.

CONSUMER RECEIVABLES: Consumer debt owed to a creditor which may be used as collateral for asset backed securities. These receivables include credit card, auto, and home equity loans.

CORPORATE NOTE: Debt instrument issued by a private corporation.

COUPON: The annual rate at which a bond pays interest.

CREDIT ANALYSIS: An analysis of the economic and financial conditions to determine creditworthiness or the ability to meet debt obligations.

CREDIT RATINGS: A grade given to a debt instrument that indicates its credit quality. Private independent rating services such as Standard & Poor's, Moody's and Fitch provide these evaluations of the issuer's financial strength, or its the ability to pay principal and interest in a timely fashion. High graded credit ratings are as follows:.

Moody's		Standard & Poor's		Fitch	
Long Term	Short Term	Long Term	Short Term	Long Term	Short Term
Aaa	P1	AAA	A1+	AAA	A1+
Aa1		AA+		AA+	
Aa2		AA		AA	
Aa3		AA-		AA-	
A1		A+	A1	A+	
A2		A		A	
A3	P2	A-	A2	A-	A2
Baa1		BBB+		BBB+	

CREDIT RISK: The risk that an obligation will not be paid and a loss will result due to a failure of the issuer of a security.

CUSIP: Stands for Committee on Uniform Securities Identification Procedures. A CUSIP number identifies most securities, including: stocks of all registered U.S. and Canadian companies, and U.S. government and municipal bonds. The CUSIP system—owned by the American Bankers Association and operated by Standard & Poor's—facilitates the clearing and settlement process of securities. The number consists of nine characters (including letters and numbers) that uniquely identify a company or issuer and the type of security.

CURRENT YIELD: The annual interest on an investment divided by the current market value. Since the 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.

CUSTODIAN: A bank or other financial institution that keeps custody of stock certificates and other assets.

DEALER: A dealer, as opposed to a broker, acts as a principal in all transactions, buying and selling for his/her own risk and account or inventory.

DEBENTURES: A bond secured only by the general credit of the issuers.

DEFEASED BOND ISSUES: Issues that have sufficient money to retire outstanding debt when due, so that the agency is released from the contracts and covenants in the bond documents.

DELIVERY VERSUS PAYMENT (DVP): Delivery of securities with a simultaneous exchange of money for the securities.

DERIVATIVE: A financial instrument that is based on, or derived from, some underlying asset, reference date, or index.

DIRECT ISSUER: Issuer markets its own paper directly to the investor without use of an intermediary.

DISCOUNT: The difference between the cost of a security and its value at maturity when quoted at lower than face value.

DIVERSIFICATION: Dividing investment funds among a variety of securities offering independent returns and risk profiles.

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

EARNED INCOME YIELD THIS PERIOD (annualized): The Total net Earnings this period divided by Average Daily Portfolio Balance and the number of days in the period, multiplied by 365 (or 360 depending on the profile setting), and then multiplied by 100.

FACE VALUE: The principal amount owed on a debt instrument. It is the amount on which interest is computed and represents the amount that the issuer promises to pay at maturity.

FAIR VALUE: The amount at which a security could be exchanged between willing parties, other than in a forced or liquidation sale. If a market price is available, the fair value is equal to the market value.

FANNIE MAE: Trade name for the Federal National Mortgage Association (FNMA), a U.S. Government sponsored enterprise.

FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC): A federal agency that provides insurance on bank deposits, guaranteeing deposits to a set limit per account, currently $100,000.

FEDERAL FARM CREDIT BANK (FFCB): Government-sponsored enterprise that consolidates the financing activities of the Federal Land Banks, the Federal Intermediate Credit Banks and the Banks for Cooperatives. Its securities do not carry direct U.S. government guarantees.

FEDERAL FUNDS RATE: The rate of interest at which Federal funds are traded. This rate is considered to be the most sensitive indicator of the direction of interest rates, as it is currently pegged by the Federal Reserve through open-market operations.

FEDERAL GOVERNMENT 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.

FEDERAL HOME LOAN BANKS (FHLB): Government sponsored enterprise (currently made up of 12 regional banks) that regulates and lends funds and provides correspondent banking services to member commercial banks, thrift institutions, credit unions and insurance companies. Although the banks operate under federal charter with government supervision, the securities are not guaranteed by the U. S. Government.

FEDERAL HOME LOAN MORTGAGE CORPORATION (FHLMC): Government sponsored enterprise that helps maintain the availability of mortgage credit for residential housing. FHLMC finances these operations by marketing guaranteed mortgage certificates and mortgage participation certificates. Its discount notes and bonds do not carry direct U.S. government guarantees.

FEDERAL NATIONAL MORTGAGE ASSOCIATION (FNMA): Government sponsored enterprise that is the largest single provider of residential mortgage funds in the United States. FNMA is a private stockholder-owned corporation. The corporation's purchases include a variety of adjustable mortgages and second loans, in addition to fixed-rate mortgages. FNMA's securities are also highly liquid and are widely accepted. FNMA securities do not carry direct U.S. Government guarantees.

FEDERAL OPEN MARKET COMMITTEE (FOMC): A committee of the Federal Reserve Board, which establishes monetary policy and executes it through temporary and permanent changes to the supply of bank reserves.

FEDERAL RESERVE SYSTEM: The central bank of the U.S. which consists of a seven member Board of Governors, 12 regional banks and about 5,700 commercial banks that are members.

FED WIRE: A wire transmission service established by the Federal Reserve Bank to facilitate the transfer of funds through debits and credits of funds between participants within the Fed system.

FREDDIE MAC: Trade name for the Federal Home Loan Mortgage Corporation (FHLMC), a U.S. government sponsored enterprise.

FITCH INDIVIUAL BANK RATINGS: Individual Ratings are assigned to banks that are legal entities. These ratings, which are internationally comparable, attempt to assess how a bank would be viewed if it were entirely independent and could not rely on external support. These ratings are designed to assess a bank's exposure to, appetite for, and management of risk, and thus represent the agency's view on the likelihood that it would run into significant financial difficulties such that it would require support. The ratings are as follows:

A: A very strong bank.
Characteristics may include outstanding profitability and balance sheet integrity, franchise, management, operating environment or prospects.

B: A strong bank.
There are no major concerns regarding the bank. Characteristics may include strong profitability and balance sheet integrity, franchise, management, operating environment or prospects.

C: An adequate bank, which, however, possesses one or more troublesome aspects. There may be some concerns regarding its profitability and balance sheet integrity, franchise, management, operating environment or prospects.

D: A bank that has weaknesses of internal and/or external origin.
There are concerns regarding its profitability and balance sheet integrity, franchise, management, operating environment or prospects. Banks in emerging markets are necessarily faced with a greater number of potential deficiencies of external origin.

E: A bank with very serious problems, which either requires or is likely to require external support.

F: A bank that has either defaulted or, in Fitch Ratings' opinion, would have defaulted if it had not received external support. Examples of such support include state or local government support, (deposit) insurance funds, acquisition by some other corporate entity or an injection of new funds from its shareholders or equivalent.

Note: Gradations may be used among the ratings A to E: i.e. A/B, B/C, C/D, and D/E. No gradations apply to the F rating.

GINNIE MAE: Trade name for the Government National Mortgage Association (GNMA), a direct obligation bearing the full faith and credit of the U.S. Government.

GOVERNMENT ACCOUNTING STANDARDS BOARD (GASB): A standard-setting body, associated with the Financial Accounting Foundation, which prescribes standard accounting practices for governmental units.

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

INACTIVE DEPOSITS: Funds not immediately needed for disbursement.

INTEREST RATE: The annual yield earned on an investment, expressed as a percentage.

INTEREST RATE RISK: The risk of gain or loss in market values of securities due to changes in interest-rate levels. For example, rising interest rates will cause the market value of portfolio securities to decline.

INVESTMENT AGREEMENTS: A contract providing for the lending of issuer funds to a financial institution which agrees to repay the funds with interest under predetermined specifications.

INVESTMENT GRADE (LONG TERM RATINGS): The minimum, high quality ratings for long term debt such as corporate notes. Investment Grade ratings are as follows: A3 (Moody's), A- (S&P), and A- (Fitch).

INVESTMENT PORTFOLIO: A collection of securities held by a bank, individual, institution or government agency for investment purposes.

LIQUIDITY: A liquid asset is one that can be converted easily and rapidly into cash with minimum risk of principal.

LOCAL AGENCY INVESTMENT FUND (LAIF): An investment pool sponsored by the State of California and administered/managed by the State Treasurer. Local government units, with consent of the governing body of that agency, may voluntarily deposit surplus funds for the purpose of investment. Interest earned is distributed by the State Controller to the participating governmental agencies on a quarterly basis.

LOCAL AGENCY INVESTMENT POOL: A pooled investment vehicle sponsored by a local agency or a group of local agencies for use by other local agencies.

MARK TO MARKET: Current value of securities at today's market price.

MARKET RISK: The risk that the value of securities will fluctuate with changes in overall market conditions or interest rates. Systematic risk of a security that is common to all securities of the same general class (stocks, bonds, notes, money market instruments) and cannot be eliminated by diversification (which may be used to eliminate non-systematic risk).

MARKET VALUE: The price at which a security is currently being sold in the market. See FAIR VALUE.

MASTER REPURCHASE AGREEMENT: A written contract covering all future transactions between the parties to repurchase agreements and reverse repurchase agreements that establish each party's rights in the transactions. A master agreement will often specify, among other things, the right of the buyer-lender to liquidate the underlying securities in the event of default by the seller-borrower.

MATURITY: The date that the principal or stated value of a debt instrument becomes due and payable.

MEDIUM-TERM NOTES (MTNs): Unsecured, investment-grade senior debt securities of major corporations which are sold in relatively small amounts either on 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. This is a measure of a portfolio's or security's exposure to market risk.

MONEY MARKET: The market in which short term debt instruments (Treasury Bills, Discount Notes, Commercial Paper, Banker's Acceptances and Negotiable Certificates of Deposit) are issued and traded.

MORTGAGED BACKED SECURITIES: A type of security that is secured by a mortgage or collection of mortgages. These securities typically pay principal and interest monthly.

MUNICIPAL BONDS: Debt obligations issued by states and local governments and their agencies, including cities, counties, government retirement plans, school districts, state universities, sewer districts, municipally owned utilities and authorities running bridges, airports and other transportation facilities

MUTUAL FUND: An entity that pools money and can invest in a variety of securities which are specifically defined in the fund's prospectus.

NEGOTIABLE CERTIFICATE OF DEPOSIT: A large denomination certificate of deposit which can be sold in the open market prior to maturity.

NET PORTFOLIO YIELD: Calculation in which the 365-day basis equals the annualized percentage of the sum of all Net Earning during the period divided by the sum of all Average Daily Portfolio Balances.

NEW ISSUE: Term used when a security is originally "brought" to market.

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

OPEN MARKET OPERATIONS: Purchases and sales of government and certain other securities in the open market by the New York Federal Reserve Bank as directed by the FOMC in order to influence the volume of money and credit in the economy. Purchases inject reserves into the bank system and stimulate growth of money and credit: Sales have the opposite effect. Open market operations are the Federal Reserve's most important and most flexible monetary policy tool.

PAR VALUE: The amount of principal which must be paid at maturity. Also referred to as the face amount of a bond. See FACE VALUE.

PORTFOLIO: The collection of securities held by an individual or institution.

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

PRIMARY DEALER: A group of government securities dealers who submit daily reports of market activity and positions and monthly financial statements to the Federal Reserve Bank of New York and are subject to its informal oversight. These dealers are authorized to buy and sell government securities in direct dealing with the Federal Reserve Bank of New York in its execution of market operations to carry out U.S. monetary policy. Such dealers must be qualified in terms of reputation, capacity, and adequacy of staff and facilities.

PRIME (SHORT TERM RATING): High quality ratings for short term debt such as commercial paper. Prime ratings are as follows: P1 (Moody's), A1 (S&P), and F1 (Fitch).

PRINCIPAL: The face value or par value of a debt instrument, or the amount of capital invested in a given security.

PROSPECTUS: A legal document that must be provided to any prospective purchaser of a new securities offering registered with the Securities and Exchange Commission that typically includes information on the issuer, the issuer's business, the proposed use of proceeds, the experience of the issuer's management, and certain certified financial statements (also known as an "official statement").

PRUDENT INVESTOR STANDARD: A standard of conduct for fiduciaries.–Investments shall be made with judgment and care--under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

PUBLIC DEPOSITS: A bank that is qualified under California law to accept a deposit of public funds.

PURCHASE DATE: The date in which a security is purchased for settlement on that or a later date. Also known as the "trade date".

RATE OF RETURN: 1) The yield which can be attained on a security based on its purchase price or its current market price. 2) Income earned on an investment, expressed as a percentage of the cost of the investment.

REALIZED GAIN (OR LOSS): Gain or loss resulting from the sale or disposal of a security.

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 or REPO): A transaction in which a counterparty or the holder of securities (e.g. investment dealer) sells these securities to an investor (e.g. the City) with a simultaneous agreement to repurchase them at a fixed date. The security "buyer" (e.g. the City) in effect lends the "seller" money for the period of the agreement, and the terms of the agreement are structured to compensate the "buyer" for this. Dealers use RP extensively to finance their positions. Exception: When the Fed is said to be doing RP, it is lending money, that is, increasing bank reserves.

REVERSE REPURCHASE AGREEMENT (REVERSE REPO): The opposite of a repurchase agreement. A reverse repo is a transaction in which the City sells securities to a counterparty (e.g. investment dealer) and agrees to repurchase the securities from the counterparty at a fixed date. The counterparty in effect lends the seller (e.g. the City) money for the period of the agreement with terms of the agreement structured to compensate the buyer.

RISK: Degree of uncertainty of return on an asset.

SAFEKEEPING: A service which banks offer to clients for a fee, where physical securities are held in the bank's vault for protection and book-entry securities are on record with the Federal Reserve Bank or Depository Trust Company in the bank's name for the benefit of the client. As agent for the client, the safekeeping bank settles securities transactions, collects coupon payments, and redeems securities at maturity or on call date, if called.

~~**SALLIE MAE:** Trade name for the Student Loan Market Association (SLMA), a U.S. government sponsored enterprise.~~

SECURITIES AND EXCHANGE COMMISSION (SEC): Agency created by Congress to protect investors in securities transactions by administering securities legislation.

SEC RULE 15C3-1: See UNIFORM NET CAPITAL RULE.

SECONDARY MARKET: A market for the repurchase and resale of outstanding issues following the initial distribution.

SECURITIES: Investment instruments such as notes, bonds, stocks, money market instruments and other instruments of indebtedness or equity.

SETTLEMENT DATE: The date on which a trade is cleared by delivery of securities against funds.

SPREAD: The difference between two figures or percentages. It may be the difference between the bid (price at which a prospective buyer offers to pay) and asked (price at which an owner offers to sell) prices of a quote, or between the amount paid when bought and the amount received when sold.

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.

STUDENT LOAN MARKET ASSOCIATION (SLMA): Government-sponsored enterprise that purchases student loans from originating financial institutions and provides financing to state student loan agencies. It provides a national secondary market for federally-sponsored student loans and credit to participants in the post secondary education lending sector.

SUBORDINATED DEBT: Debt over which senior debt has priority. In the event of a bankruptcy, subordinated debt holders receive payment only after senior debt holders are paid in full.

TIME DEPOSIT: A deposit with a California bank or savings and loan association for a specific amount and with a specific maturity date and interest rate. Deposits of up to $100,000 are insured by FDIC. Deposits over $100,000 are collateralized above the insurance with either government securities (at 110% of par value), first trust deeds (at 150% of par value), or letters of credit (at 105% of par value).

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, and includes interest earnings and realized and unrealized gains and losses on the portfolio. For bonds held to maturity, total return is the yield to maturity.

TRUSTEE OR TRUST COMPANY OR TRUST DEPARTMENT OF A BANK: A financial institution with trust powers which acts in a fiduciary capacity for the benefit of the bondholders in enforcing the terms of the bond contract.

UNDERWRITER: A dealer which purchases a new issue of municipal securities for resale.

UNIFORM NET CAPITAL RULE: Securities and Exchange Commission requirement that member firms as well as nonmember broker/dealers in securities maintain a maximum ratio of indebtedness to liquid capital of 15 to 1; also called *net capital rule* and *net capital ratio.* Indebtedness covers all money owed to a firm, including margin loans and commitments to purchase securities, one reason new public issues are spread among members of underwriting syndicates. Liquid capital includes cash and assets easily converted into cash.

U.S. GOVERNMENT AGENCY SECURITIES: Securities issued by U.S. government agencies, most of which are secured only by the credit worthiness of the particular agency. See AGENCIES.

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 the benchmark for interest rates on all other securities in the U.S. The Treasury issues both discounted securities and fixed coupon notes and bonds. The income from Treasury securities is exempt from state and local, but not federal, taxes.

> **TREASURY BILLS:** Securities issued at a discount with initial maturities of one year or less. The Treasury currently issues three-month and six-month Treasury bills at regular

weekly auctions. It also issues very short-term "cash management" bills as needed to smooth out cash flows.

TREASURY NOTES: Intermediate-term coupon-bearing securities with initial maturities of one year to ten years.

TREASURY BOND: Long-term coupon-bearing securities with initial maturities of ten years or longer.

UNREALIZED GAIN (OR LOSS): Gain or loss that has not become actual. It becomes a realized gain (or loss) when the security in which there is a gain or loss is actually sold. See REALIZED GAIN (OR LOSS).

VOLATILITY: Characteristic of a security, commodity or market to rise or fall sharply in price within a short-term period.

WEIGHTED AVERAGE MATURITY: The average maturity of all the securities that comprise a portfolio that is typically expressed in days or years.

WEIGHTED AVERAGE YIELD AT THE END OF PERIOD: The summation of each investment's period-end scheduled book value multiplied by its ending sub-period yield and divided by the total scheduled book value. Investments maturing on or before the end date of the report period will not affect the weighted average yield.

WHEN ISSUED (WI): Short form of "when, as, and if issued." WI refers to a transaction made conditionally because a security, although authorized, has not yet been issued with the exception of new Treasury, Agency, and Corporate issuances to settle within ~~14~~21 days.

YIELD: The annual rate of return on an investment expressed as a percentage of the investment. See CURRENT YIELD; YIELD TO MATURITY.

YIELD CURVE: Graph showing the relationship at a given point in time between yields and maturity for bonds that are identical in every way except maturity.

YIELD TO MATURITY: Concept used to determine the rate of return if an investment is held to maturity. It takes into account purchase price, redemption value, time to maturity, coupon yield, and the time between interest payments. It is the rate of income return on an investment, minus any premium or plus any discount, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond, expressed as a percentage.