

ADMINISTRATIVE POLICY AND PROCEDURE

SUBJECT: STATEMENT OF INVESTMENT POLICY

DATE: December 1, 2001

AMENDED DATE: January 15, 2026

REVIEWED DATE: January 15, 2026

1.0 PURPOSE

This Statement of Investment Policy (“Investment Policy”) is intended to provide guidelines for the prudent investment of the AUTHORITY FOR CALIFORNIA CITIES EXCESS LIABILITY (“ACCEL”) temporary idle cash, and outline the policies for maximizing the efficiency of ACCEL's cash management system. The ultimate goal is to enhance the economic status of ACCEL while protecting its pooled cash.

2.0 OBJECTIVE

The ACCEL cash management system is designed to accurately monitor and forecast expenditures and revenues, thus enabling ACCEL to invest funds to the fullest extent possible.

Delegation of Authority

1. ACCEL’s authority to manage its investment program is derived from the State of California Government Code (“Government Code” or “GC”) Sections 53600 *et seq.* and ACCEL’s Governing Documents.
2. ACCEL may engage the services of one or more external investment managers to assist in the management of ACCEL’s investment portfolio in a manner consistent with ACCEL’s objectives. Such external managers may be granted discretion to purchase and sell investment securities in accordance with this Investment Policy. Such managers must be registered under the Investment Advisers Act of 1940.

3.0 POLICY

All funds will be held in the name of ACCEL, and will operate its temporary pooled idle cash investments under the Prudent Investor Rule (Civil Code Sect. 2261, *et seq.*). The execution of a jointly-developed investment strategy, as well as the day-to-day investment of ACCEL’s funds shall be the responsibility of the Investment Advisor. The ACCEL Board of Directors will determine by vote the agency/organization responsible to hold, invest, and manage its portfolio. ACCEL's investments are allowable under GC Section 53600 *et seq.*, Section 53684 [County Treasury Pools] and Section 16429.1 [Local Agency Investment Fund]), and specifically, limited to those outlined herein.

Prudence: Those persons authorized to make investment decisions on behalf of ACCEL will be considered trustees and subject to the prudent investor standard that states, “when investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency.” (GC 53600.3)

4.0 CRITERIA FOR SELECTING INVESTMENTS

The criteria for selecting investments and the order of priority are:

1. Safety. The safety and risk associated with an investment refers to the potential loss of principal, interest, or a combination of these amounts. ACCEL only operates in those investments that are considered very safe. It is the primary duty and responsibility to protect, preserve, and maintain intact investments placed in trust with the Treasurer of the designated Member on behalf of the Member Agencies of ACCEL or alternatively with a banking custodian.
2. Liquidity. This refers to the ability to "cash in" at any moment in time with a minimal chance of losing some portion of principal or interest. Liquidity is an important investment quality especially when the need for unexpected funds occurs occasionally. An adequate percentage of the portfolio should be maintained in liquid short-term securities, which can be converted to cash if necessary to meet disbursement requirements. No investment shall be for a term greater than 5 years.
3. Yield. Yield is the potential dollar earnings an investment can provide and sometimes is described as the rate of return.

5.0 ACCEL'S INVESTMENTS ARE LIMITED TO THE FOLLOWING ALLOWABLE INVESTMENTS

ACCEL’s investments are governed by California Government Code, Sections 53600 et seq. Within the investments permitted by the Code, ACCEL seeks to further restrict eligible investments to the guidelines listed below. In the event a discrepancy is found between this policy and the Code, the more restrictive parameters will take precedence.

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

In order to avoid the risks associated with investing in unfamiliar instruments, any new type of security allowed by the State of California but not listed below must be approved by the Finance Committee prior to the investment of ACCEL. All minimum credit requirements and concentration limits apply at time of purchase.

5.1 Securities of the U.S. Government

U.S. Treasuries and other government obligations for which the full faith and credit of the United States are pledged for the payment of principal and interest. There are no limits on the dollar amount or percentage that the Authority may invest in U.S. Treasuries, provided that the maximum maturity is five (5) years.

5.2 Securities of U.S. Government Agencies

Federal Agency, or United States Government-Sponsored Enterprise obligations, participations, or other instruments, including those issued by or fully guaranteed as to principal and interest by federal agencies or United States government-sponsored enterprises. There are no limits on the dollar amount or percentage that ACCEL may invest in Federal Agency or Government-Sponsored Enterprises (“GSEs”), provided that no more than 30% of ACCEL’s portfolio may be invested in any single Agency/GSE issuer, and the maximum maturity is five (5) years. Moreover, the maximum percentage of agency callable securities in the portfolio will be 20%.

5.3 Banker’s Acceptances Provided That:

- a. They are issued by institutions the short-term obligations of which are rated “A-1” or its equivalent or better by at least one Nationally Recognized Statistical Rating Organization (NRSRO); or, long-term debt obligations of which are rated in a rating category of “A” by at least one NRSRO;
- b. The maturity does not exceed 180 days; and
- c. No more than 40% of ACCEL’s total portfolio may be invested in banker’s acceptances.
- d. No more than 5% of the portfolio may be invested in any single issuer.

5.4 Commercial Paper provided that the securities are issued by an entity that meets all of the following conditions in either paragraph (a) or (b) and other requirements specified below::

- a. SECURITIES issued by corporations:
 - (i) A corporation organized and operating in the United States with assets more than \$500 million.
 - (ii) The securities are rated “A-1” or its equivalent or better by at least one NRSRO.
 - (iii) If the issuer has other debt obligations, they must be rated in a rating category of “A” or its equivalent or better by at least one NRSRO.
- b. SECURITIES issued by other entities:
 - (i)The issuer is organized within the United States as a special purpose corporation, trust, or limited liability company.

(ii)The securities must have program-wide credit enhancements including, but not limited to, overcollateralization, letters of credit, or a surety bond.
(iii)The securities are rated “A-1” or its equivalent or better by at least one NRSRO.

- No more than 25% of ACCEL’s investment assets under management may be invested in Commercial Paper. Under a provision sunseting on January 1, 2031, no more than 40% of the total portfolio may be invested in Commercial Paper if the Authority’s investment assets under management are greater than \$100,000,000.
- No more than 5% of the portfolio may be invested in any single issuer.
- The maximum maturity does not exceed 397 days.

5.5 Federally insured time deposits (Non-negotiable certificates of deposit)

state or federally chartered banks, savings and loans, or credit unions, provided that:

- The amount per institution is limited to the maximum covered under federal insurance.
- No more than 20% of the portfolio will be invested in a combination of federally insured and collateralized time deposits.
- The maximum maturity does not exceed 180 days

5.6 Time deposits (Non-negotiable certificates of deposit) in in state or federally chartered banks, savings and loans, or credit unions in excess of insured amounts which are fully collateralized with securities in accordance with California law, provided that:

- a. No more than 20% of ACCEL’s portfolio shall be invested in a combination of federally insured and collateralized time deposits;
- b. The maturity of such deposits does not exceed 180 days.

5.7 Negotiable certificates of deposit (“NCDs”) issued by a nationally or state-chartered bank, a savings association or a federal association, a state or federal credit union, or by a federally licensed or state-licensed branch of a foreign bank, provided that:

- a. The amount of the NCD insured up to the Federal Deposit Insurance Corporation (“FDIC”) limit does not require any credit ratings.
- b. Any amount above the FDIC insured limit must be issued by institutions which have short-term debt obligations rated “A-1” or its equivalent or better by at least one NRSRO; or long-term obligations rated in a rating category of “A” or its equivalent or better by at least one NRSRO.
- c. The maturity does not exceed five (5) years; and

- d. No more than 30% of the total portfolio may be invested in NCDs. No more than 5% of the portfolio may be invested in any single issuer.

5.8 Medium Term Notes

- a. The issuer is a corporation organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States.
- b. ACCEL will only purchase Medium Term Notes which are rated in a rating category of "A" or its equivalent or higher by one NRSRO with maturities of five (5) years or less.
- c. No more than 30% of the total portfolio may be invested in Medium Term Notes.
- d. No more than 5% of the portfolio may be invested in any single issuer.

5.9 Local Agency Investment Fund

The Local Agency Investment Fund ("LAIF") was established by the State to enable treasurers to place funds in a pool for investment. LAIF has been particularly beneficial to those jurisdictions with small portfolios. ACCEL's investment is limited to LAIF's statutory limits. ACCEL uses this fund for short-term liquidity, investment, and yield when rates are declining. Funds are available on demand. Interest is paid quarterly. Pursuant to review by the Finance Committee, ACCEL shall maintain a balance of funds sufficient to pay known claims payouts and other expenses for the following twelve months in LAIF or other similar funds that provide similar liquidity and security. ACCEL's Finance Committee has the authority to semiannually review and adjust the liquidity ratio with ratification by the Board.

5.10 Repurchase Agreement

Investments in repurchase agreements are allowable but must comply with current GC and may not exceed one (1) year.

Closely associated with the functioning of the Federal funds market is the negotiation of repurchase agreements. Banks may buy temporarily idle funds from a customer by selling U.S. Government or other securities with the contractual agreement to repurchase the same security on a future date determined by negotiation. For the use of funds, the customer receives an interest payment from the bank; the interest rate reflects both the prevailing demand for Federal funds and the maturity of the "repo." Repurchase Agreements are usually executed for \$100,000 or more. ACCEL will require physical delivery of the securities backing the repo to its safekeeping agent. The institution from which ACCEL purchases a repo must transfer on an ongoing basis sufficient securities to compensate for changing market conditions and to insure that adequate collateral is maintained in ACCEL safekeeping account. Generally, maturities range from 1 to 90 days with interest paid at maturity.

Note: Master Repurchase Agreement required

5.11 Mutual Funds

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

- a. **Mutual Funds** that invest in the securities and obligations as authorized under California Government Code, Section 53601 (a) to (k) and (m) to (q) inclusive and that meet either of the following criteria:
 - (i) Attained the highest ranking or the highest letter and numerical rating provided by not less than two (2) NRSROs; or
 - (ii) Have retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience investing in the securities and obligations authorized by California Government Code, Section 53601 and with assets under management in excess of \$500 million.
 - No more than 10% of the total portfolio may be invested in shares of any one mutual fund.
- b. **Money Market Mutual Funds** registered with the Securities and Exchange Commission under the Investment Company Act of 1940 and issued by diversified management companies and meet either of the following criteria:
 - (i) Have attained the highest ranking or the highest letter and numerical rating provided by not less than two (2) NRSROs; or
 - (ii) Have retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience managing money market mutual funds with assets under management in excess of \$500 million.
 - No more than 20% of the total portfolio may be invested in the shares of any one Money Market Mutual Fund.
 - No more than 20% of the total portfolio may be invested in mutual funds and money market mutual funds combined.

5.12 Municipal Securities:

These include obligations of the Agency, the State of California, and any local Agency within the State of California, provided that:

- a. Long-term obligations are rated in the rating category of "A" or its equivalent or higher by at least one NRSRO;

- b. The maximum maturity is five years; and
- c. No more than 5% per issuer and municipal securities combined may not exceed 30% of the portfolio.

5.13 Municipal Securities (Registered Treasury Notes or Bonds), of any of the other 49 states in addition to California, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of any of the other 49 states, in addition to California.

- a. Long-term obligations are rated in the rating category of “A” or its equivalent or higher by at least one NRSRO;
- b. The maximum maturity is five (5) years; and
- c. No more than 5% per issuer and municipal securities combined may not exceed 30% of the portfolio.

5.14 Mortgage-Backed, Mortgage Pass-Through Securities, Collateralized Mortgage Obligations, and Asset-Backed Securities, From issuers not defined in Sections 5.1 and 5.2 of the Allowable Investments Section, Provided That:

- a. Have a maximum stated final maturity of five (5) years;
- b. Be rated in a rating category of “AA” or its equivalent or better by one NRSRO; and
- c. Purchase of securities authorized by this subdivision may not exceed 5% per issuer and 20% of the portfolio.

5.15 Supranational Securities Provided That:

- a. Issues are unsubordinated obligations issued by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank.
- b. The securities are rated “AA” or higher by one NRSRO.
- c. No more than 30% of the total portfolio may be invested in these securities.
- d. No more than 10% of the portfolio per issuer
- e. The maximum maturity does not exceed five (5) years

5.16 Shares of Beneficial Interest Issued by a Joint Powers Authority (JPA), provided that:

- a. The JPA is organized pursuant to California Government Code Section 6509.7 and invests in the securities and obligations authorized in subdivisions (a) to (r), inclusive.
- b. Each share shall represent an equal proportional interest in the underlying pool of securities owned by the JPA.
- c. The JPA has retained an investment advisor who is registered with the SEC (or exempt from registration), has assets under management in excess of \$500 million, and has at least five years' experience investing in instruments authorized by Section 53601, subdivisions (a) to (q).

6.0 PROHIBITED INVESTMENTS

GC Section 53601.6(a) outlines the types of investments that are not allowed for a local agency and is stated here:

53601.6(a) A local agency shall not invest any funds pursuant to this article in inverse floaters, range notes or mortgage derived interest-only strips. (b) A local agency shall not invest any funds pursuant to this article in any security that could result in zero interest accrual if held to maturity. Under a provision sunseting on January 1, 2031, securities backed by the U.S. Government that could result in a zero- or negative-interest accrual if held to maturity are permitted. Moreover, a local agency may hold prohibited instruments until their maturity dates. The limitation in this subdivision shall not apply to local agency investments in shares of beneficial interest issued by diversified management companies registered under the Investment Company Act of 1940 (15 U.S.C. Sec. 80a-1, and following) that are authorized for investment pursuant to subdivision (l) of Section **53601**.

Reverse Re-purchase agreements, derivative products, and any others unless allowable under Section 4.0 are also prohibited. Security purchases with a forward settlement date exceeding 45 days from the time of investment are prohibited.

7.0 REPORTS

ACCEL will be supplied quarterly reports of investment (GC Section 53646) and monthly transaction (GC Section 53607) as required by State of California.

8.0 SAFEKEEPING AND COMPETITIVE TRANSACTIONS

Securities purchased from brokers/dealers shall be held in third party safekeeping by the trust department of ACCEL's bank or other designated third party safekeeping by the trust department of ACCEL's bank or other designated third party trust, in ACCEL's name and control. "All investment transactions of the Authority shall be conducted using standard delivery-vs.-payment procedures."

All investment transactions will be conducted on a competitive basis which can be executed through a bidding process involving at least three separate brokers/financial institutions or through the use of a nationally recognized trading platform.

9.0 CONSTRAINTS

ACCEL will operate its pooled idle cash investments under the Prudent Investor Rule. This affords a broad spectrum of investment opportunities so long as the investment is deemed prudent and is permissible under currently effective legislation of the State of California and other imposed legal restrictions.

LAIF shall be used as a management tool in ACCEL's overall investment strategy.

10.0 RELATIONSHIP WITH FINANCIAL INSTITUTION

1. The ACCEL Board shall determine which financial institutions are authorized to provide investment services to ACCEL based on credit worthiness and experience of the institutions. Institutions eligible to transact investment business with ACCEL include:
 - a) Primary government dealers as designated by the Federal Reserve Bank;
 - b) Non-primary and regional dealers;
 - c) Nationally or state-chartered banks;
 - d) The Federal Reserve Bank; and,
 - e) Direct issuers of securities eligible for purchase by ACCEL.
2. Selection of financial institutions and broker/dealers authorized to engage in transactions with ACCEL shall be at the sole discretion of the ACCEL Board.
3. All financial institutions which desire to become qualified bidders for investment transactions (and which are not dealing only with the investment adviser) must supply the ACCEL Board a statement certifying that the institution has reviewed the California GC Section 53600 *et seq.* and ACCEL's Investment Policy and that all securities offered to ACCEL shall comply fully and in every instance with all provisions of the Code and with this Investment Policy.
4. Public deposits shall be made only in qualified public depositories within the State of California as established by State law. Deposits shall be insured by the Federal Deposit Insurance Corporation, or, to the extent the amount exceeds the insured maximum, shall be collateralized with securities in accordance with State law.
5. Selection of broker/dealers used by external investment advisers retained by ACCEL shall be at the sole discretion of the investment advisers, and the advisers will make available a list of broker/dealers to the Board upon request.

11.0 INVESTMENT LIMITATIONS

Security purchases and holdings shall be maintained within statutory limits imposed by the GC. Currently GC Section 53601 maximum limits are (and/or are further limited on a per entity basis by ACCEL):

40% Bankers' Acceptances, not to exceed 180 days in maturity and no more than 5% in any one entity

25% Commercial Paper, not to exceed 397 days in maturity and no more than 5% in any one entity (Under a provision sunsetting on January 1, 2026, 40% of the total portfolio may be invested in Commercial Paper if the Authority's investment assets under management are greater than \$100,000,000.

30% Negotiable Certificates of Deposit and no more than 5% in any one entity

30% Medium-Term Corporate Notes and no more than 5% in any one entity

30% Municipal Securities, no more than 5% in any one entity

20% combined in Mortgage pass-through securities, collateralized mortgage obligations, and asset-backed securities and no more than 5% in any one entity

11.1 Mitigating credit risk in the portfolio

Credit risk is the risk that a security or a portfolio will lose some or all of its value due to a real or perceived change in the ability of the issuer to repay its debt.

ACCEL shall mitigate credit risk by adopting the following strategies:

1. The diversification requirements included in Section 11.0 are designed to mitigate credit risk in the portfolio;
2. No more than 5% of the total portfolio may be invested in securities of any single issuer unless otherwise specified in this policy;
3. ACCEL may elect to sell a security prior to its maturity and record a capital gain or loss in order to improve the quality, liquidity, or yield of the portfolio in response to market conditions or ACCEL's risk preferences; and
4. If securities owned by ACCEL are downgraded to a level below the quality required by this Investment Policy, it shall be ACCEL's policy to review the credit situation and make a determination as to whether to sell or retain such securities in the portfolio.
 - a. If a security is downgraded two grades below the level required by ACCEL, the security shall be sold immediately.
 - b. If a security is downgraded one grade below the level required by this Investment Policy, ACCEL's Treasurer will use discretion in determining whether to sell or hold the security based on its current maturity, the loss in value, the economic outlook for the issuer, and other relevant factors.
 - c. If a decision is made to retain a downgraded security in the portfolio, its presence in the portfolio will be monitored and reported monthly to the ACCEL Board.

11.2 Mitigating market risk in the portfolio

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

1. The maximum stated final maturity of individual securities in the portfolio shall be five years, except as otherwise stated in this policy; Where this policy does not specify a limitation on the term or remaining maturity at the time of the investment, no investment shall be made in any security that at the time of the investment has a term remaining to maturity in excess of five years, unless the ACCEL Board of Directors has granted express authority to make that investment either specifically or as a part of an investment program approved by the Board no less than three months prior to the investment.
2. ACCEL shall maintain a minimum of three months of budgeted operating expenditures in short term investments; and
3. The duration of the portfolio typically will be equal to the duration of an index of U.S. Treasury and Federal Agency Securities with maturities which meet ACCEL's needs for cash flow and level of risk tolerance (the Benchmark Index) plus or minus 10%.

12.0 LIQUIDITY

The marketability of a security should be considered at the time of purchase, as the security may have to be sold at a later date to meet unanticipated cash demands.

13.0 LONG-TERM MATURITIES

To the extent possible, investments shall be matched with anticipated cash flow requirements and known future liabilities.

ACCEL will not invest in securities maturing more than five (5) years from the date of trade settlement, unless the Board has by resolution granted authority to make such an investment. As a general rule, long-term maturities should not represent a significant percentage of the total portfolio, as the principal risk involved can outweigh the potential for higher earnings. There should be an overall maximum allowable weighted average maturity of no more than 36 months, or duration of pool.

ACCEL strives to maintain the level of investment of all funds as near 100% as possible, through daily and projected cash flow determinations. Idle cash management and investment transactions are the responsibility of the Treasurer or equivalent of the Investment Advisor.

The basic premise underlying ACCEL's investment philosophy is, and will continue to be, to insure that money is always safe and available when needed.

14.0 ETHICS AND CONFLICT OF INTEREST CODE

Officers and employees involved in the investment process shall refrain from personal business activities that could conflict with proper execution of the investment program or which could impair their ability to make impartial decisions.

15.0 INVESTMENT POLICY ADOPTION

The policy shall be reviewed annually by the ACCEL Board and any modifications made thereto must be approved by the Board.

16.0 FINANCE COMMITTEE

At least once a year, the Finance Committee shall discuss the status of current investments, strategies for future investment, and other matters deemed relevant. If recommendations result from these reviews, action may be taken by the Board.

17.0 BENCHMARK COMPARISON

Benchmark Index. ACCEL shall monitor and evaluate the portfolio's performance relative to the chosen market benchmark(s). ACCEL shall select an appropriate, readily available index to use as a market benchmark. Any proposed changes in ACCEL's benchmark must be approved by the Board. The Investment Advisor will inform the Program Administrators of any proposed changes.

Overall objective. The investment portfolio shall be designed with the overall objective of obtaining a yield-to-maturity and total rate of return throughout economic cycles, commensurate with investment risk constraints and cash flow needs.

18.0 COMMITTEE ADVISEMENT

Finance Committee advisement and Board changes to this policy will be immediately noticed to the Investment Advisor managing ACCEL funds. Action taken and changes will be implemented within a time frame directed by the Board or no later than 30 calendar days after notice.

Glossary of Investment Terms

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

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

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

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

FNMA. Like FHLB and FreddieMac, the Federal National Mortgage Association was established to provide credit and liquidity in the housing market. FNMA, also known as “FannieMae,” issues discount notes, bonds and mortgage pass-through securities.

GNMA. The Government National Mortgage Association, known as “GinnieMae,” issues mortgage pass-through securities, which are guaranteed by the full faith and credit of the U.S. Government.

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

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

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

ASSET BACKED SECURITIES. Securities supported by pools of installment loans or leases or by pools of revolving lines of credit.

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

BANKER’S ACCEPTANCE. A money market instrument created to facilitate international trade transactions. It is highly liquid and safe because the risk of the trade transaction is transferred to the bank which “accepts” the obligation to pay the investor.

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

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

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

CALLABLE. A callable security gives the issuer the option to call it from the investor prior to its maturity. The main cause of a call is a decline in interest rates. If interest rates decline since an issuer issues securities, it will likely call its current securities and reissue them at a lower

rate of interest. Callable securities have reinvestment risk as the investor may receive its principal back when interest rates are lower than when the investment was initially made.

CERTIFICATE OF DEPOSIT (CD). A time deposit with a specific maturity evidenced by a certificate. Large denomination CDs may be marketable.

CERTIFICATE OF DEPOSIT ACCOUNT REGISTRY SYSTEM (CDARS). A private placement service that allows local agencies to purchase more than \$250,000 in CDs from a single financial institution (must be a participating institution of CDARS) while still maintaining FDIC insurance coverage. CDARS is currently the only entity providing this service. CDARS facilitates the trading of deposits between the California institution and other participating institutions in amounts that are less than \$250,000 each, so that FDIC coverage is maintained.

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

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

COMMERCIAL PAPER. The short-term unsecured debt of corporations.

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

COUPON. The rate of return at which interest is paid on a bond.

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

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

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

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

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

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

DISCOUNT. The difference between the par value of a bond and the cost of the bond, when the cost is below par. Some short-term securities, such as T-bills and banker's acceptances, are known as discount securities. They sell at a discount from par and return the par value to

the investor at maturity without additional interest. Other securities, which have fixed coupons, trade at a discount when the coupon rate is lower than the current market rate for securities of that maturity and/or quality.

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

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

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

FEDERAL OPEN MARKET COMMITTEE. A committee of the Federal Reserve Board that establishes monetary policy and executes it through temporary and permanent changes to the supply of bank reserves.

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

LIQUIDITY. The speed and ease with which an asset can be converted to cash.

LOCAL AGENCY INVESTMENT FUND (LAIF). A voluntary investment fund open to government entities and certain non-profit organizations in California that is managed by the State Treasurer's Office.

LOCAL GOVERNMENT INVESTMENT POOL. Investment pools that range from the State Treasurer's Office Local Agency Investment Fund (LAIF) to county pools, to Joint Powers Authorities (JPAs). These funds are not subject to the same SEC rules applicable to money market mutual funds.

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

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

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

MARKET VALUE. The price at which a security can be traded.

MARKING TO MARKET. The process of posting current market values for securities in a portfolio.

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

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

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

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

MORTGAGE PASS-THROUGH SECURITIES. A securitized participation in the interest and principal cash flows from a specified pool of mortgages. Principal and interest payments made on the mortgages are passed through to the holder of the security.

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

MUTUAL FUND. An entity which pools the funds of investors and invests those funds in a set of securities which is specifically defined in the fund's prospectus. Mutual funds can be invested in various types of domestic and/or international stocks, bonds, and money market instruments, as set forth in the individual fund's prospectus. For most large, institutional investors, the costs associated with investing in mutual funds are higher than the investor can obtain through an individually managed portfolio.

NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATION (NRSRO).

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

NEGOTIABLE CD. A short-term debt instrument that pays interest and is issued by a bank, savings or federal association, state or federal credit union, or state-licensed branch of a foreign bank. Negotiable CDs are traded in a secondary market and are payable upon order to the bearer or initial depositor (investor).

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

PREPAYMENT SPEED. A measure of how quickly principal is repaid to investors in mortgage securities.

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

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

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

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

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

REPURCHASE AGREEMENT. Short-term purchases of securities with a simultaneous agreement to sell the securities back at a higher price. From the seller's point of view, the same transaction is a reverse repurchase agreement.

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

STRUCTURED NOTE. A complex, fixed income instrument, which pays interest, based on a formula tied to other interest rates, commodities or indices. Examples include inverse floating rate notes which have coupons that increase when other interest rates are falling, and which fall when other interest rates are rising, and "dual index floaters," which pay interest based on the relationship between two other interest rates - for example, the yield on the ten-year Treasury note minus the Libor rate. Issuers of such notes lock in a reduced cost of borrowing by purchasing interest rate swap agreements.

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

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

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

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

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

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

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

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