CITY OF MURRIETA
INVESTMENT POLICY

I - INTRODUCTION

The City Council of the City of Murrieta (City) has adopted this Investment Policy (Policy) in order to establish the investment scope, objectives, delegation of authority, standards of prudence, reporting requirements, internal controls, eligible investments and transactions, diversification requirements, risk tolerance, and safekeeping and custodial procedures for the investment of the funds of the City. All such funds will be invested in accordance with this Policy and with applicable sections of the California Government Code. This Policy was endorsed and adopted by the City and is effective as of the 18th day of April 2023, and replaces any previous versions.

II - SCOPE

This Policy applies to all operating funds of the City. Non-operating funds may be subject to other prevailing documents, such as a governing bond indenture. This policy excludes Employees Retirement and Deferred Compensation Funds. Additional funds that may be created from time to time shall be added to the City's investment portfolio (portfolio) and managed in accordance with the provisions of this Policy.

All cash shall be pooled for investment purposes. The investment income derived from the pooled investment account shall be allocated to the contributing funds based upon the proportion of the respective average balances relative to the total pooled balance in the portfolio. Investment income shall be distributed to the individual funds not less than annually.

III - OBJECTIVES

The City's funds shall be invested in accordance with the City's Municipal Code and all applicable State statutes and Federal regulations, and in a manner designed to accomplish the following objectives, which are listed in priority order:

1. Preservation of capital and protection of investment principal.
2. Maintenance of sufficient liquidity to meet anticipated cash flows.
3. Attainment of a market value rate of return.
4. Diversification to avoid incurring unreasonable market risks.

IV - DELEGATION OF AUTHORITY

The management responsibility for the City's investment program is delegated by the City Council to the Treasurer pursuant to California Government Code Section 53607 and Section 2.20.030 of the City's Municipal Code. The City Manager serves as the Treasurer. The Treasurer has delegated the authority to conduct investment transactions and to manage the operation of the portfolio to the Finance Director. These officers shall meet regularly to discuss economic and market conditions, and to plan investment strategy to meet the City's fiscal objectives. No person may engage in an investment transaction except as expressly provided under the terms of this Policy.

V - PRUDENCE

The standard of prudence to be used for managing the City's investments shall be California Government Code Section 53600.3, the prudent investor standard, which states that "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."

The City's overall investment program shall be designed and managed with a degree of professionalism that is worthy of the public trust. The City recognizes that no investment is totally without risk and that the investment activities of the City are a matter of public record. Accordingly, the City recognizes that occasional measured losses may occur in a diversified portfolio and shall be considered within the context of the overall portfolio's return, provided that adequate diversification has been implemented and that the sale of a security is in the best long-term interest of the City.

If, due to market changes or fluctuations in the size of the City's portfolio, a percentage of portfolio limitation is exceeded, the affected securities may be held to their maturity if the Treasurer believes it is prudent to do so.

The Treasurer and authorized investment personnel exercising due diligence shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided that the deviations from expectations are reported in a timely fashion to the City Council and appropriate action is taken to control adverse developments.

VI - ETHICS AND CONFLICTS OF INTEREST

Elected officials and employees involved in the City's investment program shall refrain from personal business activity that could conflict with proper execution of the investment program or that could impair or create the appearance of an impairment of their ability to make impartial investment decisions. These individuals shall disclose to the City Manager any material interests they have in financial institutions that conduct business with the City and they shall subordinate their personal investment transactions to those of the City.

The Treasurer and the Finance Director shall file a Statement of Economic Interests each year pursuant to California Government Code Section 87203 and regulations of the Fair Political Practices Commission.

VII - AUTHORIZED SECURITIES AND TRANSACTIONS

All investments and deposits of the City shall be made in accordance with California Government Code Sections 16429.1, 53600-53609 and 53630-53686, except that, pursuant to California Government Code Section 5903(e), proceeds of bonds and any moneys set aside or pledged to secure payment of the bonds may be invested in securities or obligations described in the ordinance, resolution, indenture, agreement, or other instrument providing for the issuance of the bonds. Any revisions or extensions of the above referenced code sections will be assumed to be part of this Policy immediately upon being enacted. However, in the event that amendments to these sections conflict with this Policy and past City investment practices, the City may delay adherence to the new requirements when it is deemed in the best interest of the City to do so. In such instances, after consultation with the City's attorney, the Treasurer will present a recommended course of action to the City Council for approval. Percentage holding limits and credit quality minimums listed in this section apply at the time the security is purchased.

The City has further restricted the eligible types of securities and transactions as follows:

A. **United States Treasury** bills, bonds, and notes with a final maturity not exceeding five years from the date of trade settlement. There is no limitation as to the percentage of the portfolio that can be invested in this category.

B. **Federal Agency Obligations** for which the faith and credit of the United States are pledged for the payment of principal and interest, and which have a final maturity not exceeding five years from the date of trade settlement. There is no limitation as to the percentage of the portfolio that can be invested in this category.

C. **Federal Instrumentality** (government sponsored enterprise) debentures, discount notes, callable securities and step-up securities with a final maturity not exceeding five years from the date of trade settlement. No more than 30% of the portfolio may be invested in any single Federal Instrumentality/GSE issuer. The maximum percentage of callable agency securities in the portfolio is 20%.

D. **Mortgage-backed Securities,** Collateralized Mortgage Obligations and Asset-backed Securities limited to mortgage-backed pass-through securities issued by a US government agency or consumer receivable pass-through certificates or bonds with a final maturity not exceeding five years from the date of trade settlement. The securities are rated in a rating category of "AA" or its equivalent or higher by a NRSRO. The aggregate investment in mortgage-backed and asset-backed securities described in this section shall not exceed 20% of the portfolio with no more than 5% held in any one issuer that is not a US government agency.

E. **Repurchase Agreements** with a final termination date not exceeding one year collateralized with securities authorized under California Government Code. For the purpose of this section, the term collateral shall mean purchased securities under the terms of the City's approved Master Repurchase Agreement. The purchased securities shall have a minimum market value including accrued interest of 102% of the dollar value of the funds borrowed. Collateral shall be held in the City's custodian bank, as safekeeping agent, and the market value of the collateral securities shall be marked-to-the-market daily.

Repurchase Agreements shall be entered into only with broker/dealers who are recognized as Primary Dealers by the Federal Reserve Bank of New York or with firms that have a primary dealer within their holding company structure. The Treasurer shall maintain a copy of the City's approved Master Repurchase Agreement along with a list of the broker/dealers who have executed same.

The aggregate investment in Repurchase Agreements shall not exceed 20% of the portfolio.

F. **Prime Commercial Paper** with a maturity not exceeding 270 days from the date of trade settlement with the highest ranking or of the highest letter and number rating assigned by a NRSRO. The entity that issues the commercial paper shall meet all of the conditions in either sub-paragraph 1) or sub-paragraph 2) below:

1) The entity shall (a) be organized and operating in the United States as a general corporation, (b) have total assets in excess of $500,000,000, and (c) have debt other than commercial paper, if any, that is rated in a rating category of "A" or its equivalent or higher by a NRSRO.
2) The entity shall (a) be organized within the United States as a special purpose corporation, trust, or limited liability company, (b) have program-wide credit enhancements, including, but not limited to, over collateralization, letters of credit or surety bond and (c) have commercial paper that is rated in a rating category of "A-1" or its equivalent or higher by a NRSRO.

Not more than 5% of the portfolio may be invested in the commercial paper and medium-term notes of any issuer and the aggregate investment in commercial paper shall not exceed 25% of the portfolio. Under a provision sunsetting on January 1, 2026, no more than 40% of the portfolio may be invested in Commercial Paper if the Agency's investment assets under management are greater than $100,000,000.

G. **Eligible Bankers Acceptances** issued by Federal Deposit Insurance Corporation (FDIC) insured commercial banks, rated at least "A-1" or the equivalent by a NRSRO with maturities not exceeding 180 days from the date of trade settlement. If issuers have senior debt outstanding, it shall be rated in a rating category of "A" or its equivalent or higher by a NRSRO. No more than 5% of the portfolio shall be invested in bankers acceptances of any one commercial bank, and the aggregate investment in bankers acceptances shall not exceed 30% of the portfolio.

H. **Medium-Term Notes** issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States. Medium-Term Notes shall have a final maturity not exceeding five years from the date of trade settlement and must be rated in a rating category of "A" or its equivalent or higher by a NRSRO at the time of purchase. Not more than 5% of the City's total portfolio shall be invested in the Medium-Term Notes and commercial paper of any one issuer and the aggregate investment in Medium-Term Notes may not exceed 30% of the portfolio.

I. **Supranational Securities** that are United States dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank, with a maximum remaining maturity of five years or less, and eligible for purchase and sale within the United States. Investments under this subdivision shall be rated in a rating category of “AA” or its equivalent or higher by a NRSRO and shall not exceed 30% of the portfolio with no more than 10% invested in any one issuer.

J. **State of California’s Local Agency Investment Fund (LAIF)**,
The City may invest up to the maximum amount permitted by LAIF, pursuant to California Government Code Section 16429.1. LAIF’s investments in instruments prohibited by or not specified in the City’s policy do not exclude the investment in LAIF itself from the City’s list of allowable investments, provided LAIF’s reports allow the Treasurer to adequately judge the risk inherent in LAIF’s portfolio.

K. **Municipal Bonds**, State of California registered warrants or treasury notes or bonds, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the state or by a department, board, agency, or authority of the state.

Registered treasury notes or bonds of any of the other 49 states in addition to California, including bonds payable solely out of the revenues from a revenue producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of any of the other 49 states, in addition to California.

Bonds, notes, warrants, or other evidences of indebtedness of a local agency within California including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the local agency, or by a department, board, agency, or authority of the local agency.

In addition, these securities must be rated in a rating category of “A” or its equivalent or higher by a NRSRO with maturities not exceeding five years from the date of trade settlement. No more than 5% of the portfolio shall be invested in any one municipal issuer and the aggregate investment in municipal bonds shall not exceed 30% of the portfolio.

L. **Money Market Funds** registered under the Investment Company Act of 1940 that are (1) “no-load” (meaning no commission or fee shall be charged on purchases or sales of shares); (2) have a constant net asset value per share of $1.00; (3) invest only in the securities and obligations authorized in the applicable California statute; and (4) have a rating in a rating category of “AAA” or its equivalent by at least two NRSROs. Investment in any individual fund may not exceed 10% of the fund, and the aggregate investment in any combination of Money Market Funds and Mutual Funds shall not exceed 20% of the portfolio.

M. **Mutual Funds** registered under the Investment Company Act of 1940 that are (1) "no-load" (meaning no commission or fee shall be charged on purchases or sales of shares); (2) invest only in the securities and obligations authorized in the applicable California statute; and (3) have a rating in a rating category of "AAA" or its equivalent by at least two NRSROs. The investment in any individual Mutual Fund shall not exceed 10% of the portfolio. In addition, investment in any individual fund may not exceed 10% of the fund, and the aggregate investment in any combination of Mutual Funds and money market funds shall not exceed 20% of the portfolio.

N. **Negotiable Certificates of Deposit (NCDs)**, issued by a nationally or state-chartered bank, a savings association or a federal association, a state or federal credit union, or by a federally licensed or state-licensed branch of a foreign bank, provided that: The amount of the NCD insured up to the FDIC limit does not require any credit ratings; Any amount above the FDIC insured limit must be issued by institutions which have short-term debt obligations rated "A-1" or its equivalent or better by at least one NRSRO; or long-term obligations rated in a rating category of "A" or its equivalent or higher by at least one NRSRO; No more than 30% of the total portfolio may be invested in NCDs (combined with CDARS); No more than 5% of the portfolio may be invested in any single issuer; The maximum maturity does not exceed five (5) years.

O. **Federally Insured Time Deposits (Non-Negotiable Certificates of Deposit)** in state or federally chartered banks, savings and loans, or credit unions, provided that: (1) The amount per institution is limited to the maximum covered under federal insurance; (2) No more than 20% of the portfolio will be invested in a combination of federally insured and collateralized time deposits; and (3) The maximum maturity does not exceed five (5) years.

P. **Collateralized Time Deposits (Non-Negotiable Certificates of Deposit)** in state or federally chartered banks, savings and loans, or credit unions in excess of insured amounts which are fully collateralized with securities in accordance with California law, provided that: No more than 20% of the portfolio will be invested in a combination of federally insured and collateralized time deposits; The maximum maturity does not exceed five (5) years.

Q. **Certificate of Deposit Placement Service (CDARS)** provided that: No more than 30% of the total portfolio may be invested in a combination of Certificates of Deposit, including CDARS; The maximum maturity does not exceed five (5) years.

R. **Collateralized Bank Deposits**. The City's deposits with financial institutions will be collateralized with pledged securities per California Government Code, Section 53651. There are no limits on the dollar amount or percentage that the City may invest in collateralized bank deposits.

Summary of Allowable Investments

Investment Type	State Code CGC 53601 Max Maturity	% Limit	Required Rating	City of Murrieta Policy Max Maturity	% Limit	Required Rating
US Treasury	5 years	None	None	5 years	None	None
US Agency	5 years	None	None	5 years	None	None
US Instrumentality	5 years	None	None	5 years	None	None
Mortgage and Asset Backed Securities[2]	5 years	20%	"AA"	5 years	20%	"AA"
Repurchase Agreement[4]	1 year	None	None	1 year	20%	None
Commercial Paper[1]	270 days	25%[7]	A-1/P-1	270 days	25%[7]	A-1/P-1
Bankers Acceptances[1]	180 days	40%	A-1/P-1	180 days	30%	A-1/P-1
Corporate Notes[1]	5 years	30%	"A"	5 years	30%	"A"
Supranational[1]	5 years	30%	"AA"	5 years	30%	"AA"
LAIF	N/A	LAIF Max	None	N/A	LAIF Max	None
Cal. Local Agency[1]	5 years	None	None	5 years	30%	"A"
State Bonds[1]	5 years	None	None	5 years	30%	"A"
Money Market Fund[3]	N/A	20%	Multiple	N/A	20%	"AAA"
Mutual Fund[3]	N/A	20%	Multiple	N/A	20%	Multiple
Negotiable CDs[5]	5 years	30%	None	5 years	30%	A-1/P-1
FDIC Insured TD[6]	5 years	None	None	5 years	20%	None
Time Deposits (TD)[6]	5 years	None	None	5 years	20%	"A"
CDARS[5]	5 years	30%	None	5 years	30%	None

1) All non-federal governmental securities are limited to no more than 5% per issuer, with the exception of money market funds, mutual funds, supranationals, LAIF, or unless otherwise specified in this investment policy.
2) Total of all asset backed and mortgage backed securities may not exceed 20% of the portfolio.
3) Money Market Funds must be rated "AAA" by two NRSROs, no fund can have more than 10% of the portfolio and the total of all money market and mutual funds cannot exceed 20% of the portfolio.
4) Securities held as collateral must have a value that is more than 102% of the funds invested in the repo.
5) No more than 30% of the total portfolio may be invested in NCDs (combined with CDARS)
6) No more than 20% of the portfolio will be invested in a combination of federally insured and collateralized time deposits
7) Under a provision sunsetting on January 1, 2026, no more than 40% of the portfolio may be invested in Commercial Paper if the Agency's investment assets under management are greater than $100,000,000.

VIII – MITIGATING CREDIT RISK IN THE PORTFOLIO

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

- The diversification requirements included in the "Authorized Securities and Transactions" section of this policy are designed to mitigate credit risk in the portfolio.

- The City may elect to sell a security prior to its maturity and record a capital gain or loss in order to manage the quality, liquidity or yield of the portfolio in response to market conditions or City's risk preferences.

- If a security owned by the City is downgraded to a level below the requirements of this policy, making the security ineligible for additional purchases, the following steps will be taken:

    - Any actions taken related to the downgrade by the investment manager will be communicated to the Treasurer in a timely manner.

    - If a decision is made to retain the security, the credit situation will be monitored and reported to the City Council.

The foregoing list of authorized securities and transactions shall be strictly interpreted. Any deviation from the list must be preapproved by the City Council.

IX – PROHIBITED INVESTMENT VEHICLES AND TRANSACTIONS

- State law notwithstanding, any investments not specifically described herein are prohibited, including, but not limited to futures and options.
- In accordance with California Government Code, Section 53601.6, investment in inverse floaters, range notes, or mortgage-derived interest-only strips is prohibited.
- Investment in any security that could result in a zero interest accrual if held to maturity is prohibited. Under a provision sunsetting on January 1, 2026, securities backed by the U.S. Government that could result in a zero- or negative-interest accrual if held to maturity are permitted.
- Trading securities for the sole purpose of speculating on the future direction of interest rates is prohibited.
- Purchasing or selling securities on margin is prohibited.
- The use of reverse repurchase agreements, securities lending or any other form of borrowing or leverage is prohibited.
- The purchase of foreign currency denominated securities is prohibited.
- Securities with forward settlement date exceeding 45 days from the time of the investment is prohibited.

X - INVESTMENT DIVERSIFICATION

The City shall diversify the portfolio to avoid incurring unreasonable risks inherent in over investing in specific instruments, individual financial institutions or maturities. The asset allocation in the portfolio should, however, be flexible depending upon the outlook for the economy, the securities market, and the City's anticipated cash flow needs.

XI - PORTFOLIO MATURITIES AND LIQUIDITY

To the extent possible, investments shall be matched with anticipated cash flow requirements and known future liabilities. The City will not invest in securities maturing more than five years from the date of trade settlement, unless the City Council has by resolution granted authority to make such an investment at least three months prior to the date of the investment.

XII - SELECTION OF BROKERS/DEALERS

The Treasurer shall maintain a list of broker/dealers approved for investment purposes, and it shall be the policy of the City to purchase securities only from those brokers and the firms they represent. Each approved broker/dealer must possess an authorizing certificate from the California Commissioner of Corporations as required by Section 25210 of the California Corporations Code. The firms they represent must:

1. be recognized as Primary Dealers by the Federal Reserve Bank of New York or have a primary dealer within their holding company structure, or
2. report voluntarily to the Federal Reserve Bank of New York, or
3. qualify under Securities and Exchange Commission (SEC) Rule 15c3-1 (Uniform Net Capital Rule).

The City may engage the services of investment advisory firms to assist in the management of the portfolio and investment advisors may utilize their own list of approved Broker/Dealers. Such Broker/Dealers will comply with the selection criteria above and the list of approved firms shall be provided to the City on an annual basis or upon request.

In the event that an external investment advisor is not used in the process of recommending a particular transaction in the City's portfolio each authorized broker/dealer shall be required to submit and annually update a City approved Broker/Dealer Information Request form that includes the firm's most recent financial statements.

The City may purchase Commercial Paper from direct issuers even though they are not on the approved broker/dealer list as long as they meet the criteria outlined in Item F of the Authorized Securities and Transactions section of this Policy.

XIII – COMPETITIVE TRANSACTIONS

All investment transactions shall be conducted competitively with authorized broker/dealers. At least three broker/dealers shall be contacted for each transaction and their bid or offering prices shall be recorded. When purchasing original issue securities, no competitive offerings will be required as all dealers in the selling group offer at the same new issue price.

If the City is offered a security for which there is no other readily available competitive offering, then the Treasurer will document quotations for comparable or alternative securities.

XIV - SAFEKEEPING AND CUSTODY

To protect against potential losses due to failure of individual securities dealers, and to enhance access to securities, interest payments and maturity proceeds, all cash and securities in the City's portfolio shall be held in safekeeping in the City's name by a third party custodian, acting as agent for the City under the terms of a custody agreement executed by the bank and the City. All investment transactions will require a safekeeping receipt or acknowledgment generated from the trade. A monthly report will be received by the City from the custodian listing all securities held in safekeeping with current market data and other information.

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

The purchase and sale of securities and repurchase agreement transactions shall be settled on a delivery-versus-payment basis.

XV - PORTFOLIO PERFORMANCE

The portfolio shall be designed to attain a market rate of return throughout budgetary and economic cycles, taking into account prevailing market conditions, risk constraints for eligible securities, and cash flow requirements. The performance of the portfolio shall be compared to the performance of the ICE BofAML 1-3 year Treasury Index. The duration of the portfolio will be approximately equal (+/- 20%) of the benchmark.

XVI - REPORTING

Monthly transaction reports will be submitted by the Treasurer to the City Council in accordance with California Government Code Section 53607.

Quarterly, the Treasurer shall submit to the City Council a report of the investment earnings and performance results of the portfolio within 45 days after the end of the quarter. The report shall include the following information:

1. Investment type, issuer, date of maturity, par value and dollar amount invested in all securities, and investments and monies held by the City;
2. A description of the funds, investments or programs under the management of contracted parties, including securities lending programs;
3. A market value as of the date of the report (or the most recent valuation as to assets not valued monthly) and the source of the valuation;
4. Overall portfolio yield based on historical cost;
5. Weighted average maturity;
6. A statement of the portfolio's compliance with this Investment Policy or an explanation for non-compliance; and
7. A statement of the ability or inability to meet expenditure requirements for six months, as well as an explanation of why money will not be available if that is the case.

XVII - POLICY REVIEW

This Investment Policy shall be adopted by resolution of the City Council annually. It shall be reviewed at least annually to ensure its consistency with the overall objectives of preservation of principal, liquidity, yield and diversification and its relevance to current law and economic trends. Any amendments to this Investment Policy shall be forwarded to the City Council for approval.

GLOSSARY OF INVESTMENT TERMS

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

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

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

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

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

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

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

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

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.

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, the issuer will likely call its current securities and reissue them at a lower rate of interest.

CERTIFICATE OF DEPOSIT (CD). A time deposit with a specific maturity evidenced by a certificate.

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 BANK DEPOSIT. A bank deposit that is collateralized at least 100% (principal plus interest to maturity). The deposit is collateralized using assets set aside by the issuer such as Treasury securities or other qualified collateral to secure the deposit in excess of the limit covered by the Federal Deposit Insurance Corporation.

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.

COLLATERALIZED TIME DEPOSIT. Time deposits that are collateralized at least 100% (principal plus interest to maturity). These instruments are collateralized using assets set aside by the issuer such as Treasury securities or other qualified collateral to secure the deposit in excess of the limit covered by the Federal Deposit Insurance Corporation.

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

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.

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 security to changes interest rates.

FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC). The Federal Deposit Insurance Corporation (FDIC) is an independent federal agency insuring deposits in U.S. banks and thrifts in the event of bank failures. The FDIC was created in 1933 to maintain public confidence and encourage stability in the financial system through the promotion of sound banking practices.

FEDERALLY INSURED TIME DEPOSIT. A time deposit is an interest-bearing bank deposit account that has a specified date of maturity, such as a certificate of deposit (CD). These deposits are limited to funds insured in accordance with FDIC insurance deposit limits.

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.

Maturity. The final date upon which the principal of a security becomes due and payable. The investment's term or remaining maturity is measured from the settlement date to final maturity.

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.

Money Market Mutual Fund. A mutual fund that invests exclusively in short-term securities. Examples of investments in money market funds are certificates of deposit and U.S. Treasury securities. Money market funds attempt to keep their net asset values at $1 per share.

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 Certificate of Deposit (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.

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."

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.

SECURITIES AND EXCHANGE COMMISSION (SEC). The U.S. Securities and Exchange Commission (SEC) is an independent federal government agency responsible for protecting investors, maintaining fair and orderly functioning of securities markets and facilitating capital formation. It was created by Congress in 1934 as the first federal regulator of securities markets. The SEC promotes full public disclosure, protects investors against fraudulent and manipulative practices in the market, and monitors corporate takeover actions in the United States.

SECURITIES AND EXCHANGE COMMISSION SEC) RULE 15C3-1. An SEC rule setting capital requirements for brokers and dealers. Under Rule 15c3-1, a broker or dealer must have sufficient liquidity in order to cover the most pressing obligations. This is defined as having a certain amount of liquidity as a percentage of the broker/dealer's total obligations. If the percentage falls below a certain point, the broker or dealer may not be allowed to take on new clients and may have restrictions placed on dealings with current client.

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.

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

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

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

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

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