COUNTY OF SANTA CRUZ ~~0153~~ ~~0153~~

OFFICE OF THE TREASURER-TAX COLLECTOR ~~0059~~

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March 7, 2001 Agenda: March 20, 2001

BOARD OF SUPERVISORS
County of Santa Cruz
701 Ocean Street
Santa Cruz, CA 95060

Re: Proposed 2001 Investment Policy

Dear Members of the Board:

Government Code 1648 1.2(a) requires the Treasurer to annually prepare a written statement of investment policy. This Policy is to be reviewed by the Treasury Oversight Commission and then approved by your Board. The attached Investment Policy for 200 1 was reviewed by the Treasury Oversight Commission at their regularly scheduled quarterly meeting on January 17,200 1 and per their direction, is submitted for your Board's approval, as required by Code.

The Proposed 2001 Investment Policy includes three minor changes from the 2000 version, primarily for clarification purposes. The first change is found on page 5, where the words "not less than" are added to clarify the amount of capital a broker must have. The second change is on page 1 of Exhibit B, to clarify what is included when calculating percentages. The third change is found on pages 3 and 4 of Exhibit B. The purpose of this change is to confirm and clarify the grandfathering aspects of existing investments and the recognition that the portfolio need not adjust to changes in the size or in changes of permitted securities or quality downgrades.

While successfully concluded, the investment in PG&E Corporation Commercial Paper prompted concern about the County's Investment Policy. To provide some context for the County's investments, our office has prepared a report that provides background information on the County's investments, our investment procedures, and the investment market available to local governments in general. A copy of the report is attached to this letter.

At the time the Proposed 2001 Investment Policy was reviewed and approved by the County's Treasury Oversight Commission, the Treasurer's purchase of PG&E Corporation commercial paper was known. After much discussion at their last quarterly meeting in January, the Commission concluded that the investment was made within accepted guidelines for preventing any loss of investment principal, and within the guidelines provided by the state mandated County Investment Policy. The Commission did not recommend corrections or adjustments to the Policy, as a method to guarantee that an event as unlikely as the default, however temporary, by a major corporation would not occur in the future.

However, our office wishes to assure your Board and members of the public that as much as is possible and practical, each and every issuer and each investment option will be reviewed thoroughly before any security is purchased, and consistent with the Auditor's recommendation on your Board's February 15,200 1 agenda, that the County's investment officer will consult with the County's financial advisor prior to making an investment in specific issues of commercial paper.

It is therefore RECOMMENDED that your Board approve and adopt the attached Proposed 200 1 Investment Policy.

Sincerely,

Richard W. Bedal

Richard W. Bedal
Treasurer-Tax Collector

Enclosure

The Treasurer's Responsibilities and the Investment Policy Relative to Investment Strategy and Acceptable Risk

While successfully concluded, the investment in PG&E Corporation Commercial Paper prompted some concern about the County's Investment Policy. The following report provides background information on the County's investments, procedures, and the investment market in general.

The Investment Policy

The Investment Policy establishes the methodology to be used in investing the money in the County Pool, sets requirements, limitations and qualifications for pool members and others involved with the investing process, authorizes permitted investments and describes additional related issues. The Policy is reviewed no less than annually, and may be revised to address any changes required by legislative mandate or changing circumstances. Modifications made between the annual certification by the Board require a review by the Treasury Oversight Committee and approval of the Board of Supervisors.

History of the Investment Policy

Until 1970, investment choices were few and were basically administrative in nature. Investment losses in the 1980s by a number of cities in California and the Orange County crisis in 1994 focused more attention on the investments that were permitted, as well as the role of the Treasurer. The lack of fiduciary oversight that was brought to light after the Orange County bankruptcy prompted various changes to the Government Code that governed investment policies. Among other things, these changes included the mandate that local government Boards or Councils adopt an Investment Policy, and appoint a Treasury Oversight Commission to provide input to the investment process. In Santa Cruz County, the members include an appointed representative of the Board of Supervisors, the County Superintendent of Schools, or designee, a representative selected by the presiding officers of the governing bodies of the school and community college districts, a representative selected by the presiding officers of the governing bodies of the special districts that are required or authorized to deposit funds into the Investment Pool, and a member of the public with expertise in, or an academic background in public finance.

Although the Santa Cruz County Treasurer has had an Investment Policy for decades, it was not until 1996 that each county's Board of Supervisors was required to adopt and approve a Policy as prepared by the County Treasurer.

Purpose of Investment Pool and Role of the Treasurer

The inflow of revenues to local government agencies rarely matches the timing of their obligatory expenditures. For example, the main source of county funding, property tax revenues, are obtained from semiannual installments, while local agency payroll obligations and other similar spending commitments occur much more frequently throughout the year. Various local agencies often receive "lump-sum" proceeds from the sale of bonds or notes issued to cover shortfalls, or to pay for capital improvements-these proceeds are not expended immediately, but rather are dispersed over a period of several months or even years.

The Treasurer's ability to invest these idle cash balances pending expenditure provides significant interest earnings to the Investment Pool participants. Interest earnings not only add to the funds available to meet the needs of the local agency, but also pay for all banking and other treasury related services.

Under the current laws of the State of California, it is the responsibility of the County Treasurer, at the direction of the Board of Supervisors, to secure and protect the public funds of the County and the participants of the Investment Pool, and to establish proper safeguards, controls and procedures to maintain these funds in a lawful, rational and auspicious manner. The County Treasurer also acts as the Treasurer, cash manager, and investor for a sizable number of public agencies within the County, rather than each entity separately having to locate and hire a knowledgeable person to handle the entity's banking, investments, and other financial duties. The pooling of public funds by Investment Pool participants is aimed to eliminate duplication of expenses, smooth out cash flow, permit cost savings through higher volume, and attract professional investment service providers.

Cash Management

A major part of the Treasurer's investment responsibilities is to be certain there are sufficient funds in the County's checking account to cover all the checks that have been issued. At the same time, leaving too much in a non-or-low interest bearing checking account results in reduced yield. However, the cash management system should, above all else, ensure that cash is available to support operations.

Cash management may be defined as all activities undertaken to insure maximum cash availability and maximum investment yield on a government's idle cash. Idle cash is only idle and available to invest until it is needed to pay employees or invoices. An important objective of an effective cash management program is to time investments so that they mature at the same time they are needed to meet these obligations. If they mature too early, the county is losing interest earnings. If they mature too late, the county risks a potentially damaging problem of illiquidity, or not having cash available to meet obligations due. The Treasurer also allows for a margin of unexpected expenditures.

As described below, there are a variety of investment instruments with different yields, maturities and liquidity to assist the Treasurer in meeting the cash flow needs of the county.

Investment Instruments in the Fixed Income Market

The financial markets are globally interconnected markets for a vast array of financial securities including common stocks, bonds, short-term credit instruments, currencies and precious metals, commodities, mortgages, etc. While there is a wide range of fixed income products designed to meet the different needs of particular issuers and investors, under State Government Codes, California local agency Treasurers are restricted to only the highest quality and safest types of securities and investment agreements -- Treasury, Agency, and certain bank and corporate debt issues. These are described below:

United States Treasury Securities (Treasuries). U.S. Treasury Bills, Treasury Notes and Bonds are securities issued by the government to fund and manage the federal debt. These are backed by the full faith and credit of the U.S. Government. Local Agencies in California are legally permitted to invest in any of these securities, though normally local agencies invest in those with maturities under five years.

Federal Agencies (Agencies). Federally-sponsored Agencies of the United States Government also issue short-term discount securities and interest-bearing notes and bonds. These agencies were created by Congress to reduce the cost of capital for certain borrowing sectors of the economy deemed to be important enough to the common good of the citizenry to warrant government assistance, such as farmers, homeowners, small businesses, students and other service providers. There are two forms of Federal Agencies now in existence: those that have special drawing rights at the U.S. Treasury, thus having *de facto* backing from the federal government; and, those Agencies that have been privatized, and no longer possess such drawing rights. Even the latter are considered very secure, as some government connection is still assumed and most financial experts agree that Congress would financially support these Agencies since they provide services that Congress believes is essential. Local agencies in California are legally permitted to invest in any of these securities, though again, generally only in maturities under five years.

Commercial Paper (CP) Commercial paper is a short-term, unsecured obligation issued by both financial and non-financial companies to help satisfy their short-term funding needs. High quality utility, financial and industrial companies as well as foreign banks, and even sovereign entities are able to issue CP. CP is issued for a specific face amount that matures on a specific future date, and is typically sold on a discounted basis. The maximum maturity for most CP is 270 days, with the majority of all issuances maturing in under 90 days. Rating agencies assign ratings to CP issuers indicating their assessment of the short-term credit risk associated with each issuer. In order to receive investment grade ratings, a CP issuer must demonstrate alternative liquidity to pay maturing CP notes independent of issuing new commercial paper. Local Agencies in California are legally permitted to invest only in CP of the top rating category, A- l/P- 1, and the County's Investment Policy allows investment only in issuances which mature in 90 or fewer days.

Negotiable Certificates of Deposit (CDs) Negotiable certificates of deposit are marketable receipts for funds deposited in a bank for a fixed time period at a stated rate of interest. Negotiable CDs are most often issued in $1 ,OOO,OOO increments with maturities from one month and longer, though relatively few are issued for periods beyond one year. CDs issued by domestic banks may be insured by the Federal Deposit Insurance Corporation" (FDIC) up to $100,000, but many carry no such coverage at all. Negotiable CDs issued in bank branches in the U.S. or by U.S. bank branches in other countries for maturities under five years are permissible investments for local agencies.

Banker's Acceptances (BAs) Banker's Acceptances are time drafts or bills of exchange that are accepted for payment by banks engaged in the financing of international trade. BAs have traditionally financed the importation, exportation, shipment or storage of foreign and domestic goods, and are backed by documentation such as invoices, bills of lading, or warehouse receipts. Upon acceptance by a bank, a BA becomes an irrevocable and unconditional obligation of the accepting bank, while it is also an obligation of the drawer as well as any endorser thereof. BAs are one of the highest quality securities permitted for investment by local agencies; however, these securities are infrequently available.

Medium Term Notes (MTNs) Medium Term Notes are unsecured corporate debt obligations offered in a broad range of maturities, though primarily in the one to five year maturity range. MTNs were created to bridge the gap between commercial paper and corporate bonds. They can be floating or fixed rate, and are usually noncallable, unsecured debt obligations. Local agencies may purchase investment grade, rated A or higher, that mature under five years, with some additional qualifications.

Repurchase Agreements (Repos) Repurchase agreements are transactions in which a client purchases a security while at the same time agreeing to sell it back at the same price on a specific date with a specific interest rate paid for the time owned. In effect, a financial institution receives cash and provides securities as collateral. At termination, the client receives the cash back, with accrued interest based upon an agreed rate, and returns the securities to the financial institution. Brokerage firms use these agreements to finance the securities in their trading portfolios. The term of a repurchase agreement may be any length from overnight to one year. The overnight repo offers daily liquidity, and because repos are fully collateralized, they offer a high degree of safety and quite frequently, a competitive yield.

Other Investment Types. The State Government Codes also permit other investment types, including certain tax-free municipal issues, money market mutual funds, mortgage backed securities and even some options and future contracts. For the most part these are only prudent under special circumstances and the County's Investment Policy prohibits or greatly restricts investment in these security types at this time.

Defining Risk

Risk is inherent throughout the investment process. There is risk assigned to any investment activity as well as opportunity risk related to investment inactivity. Risks is generally associated with the following categories:

Market Risk. Market risk is derived from exposure to overall changes in the general level of interest rates. The market value of a security varies inversely with the level of interest rates. If an investor is required to sell an investment with a 5 percent yield in a comparable 7 percent rate environment, that security will be sold at a loss. The magnitude of that loss will depend on the amount of time until maturity. Market risk can be minimized through careful scrutiny of potential purchases, proper cash flow analysis, and diversification.

Interest-Rate Risk. The single most important factor in understanding fluctuations in the bond market is the impact that changes in the prevailing level of interest rates have on the market value of all outstanding bonds. When interest rates decline, bond prices rise; and when interest rates rise, bond prices decline. A typical bond is issued with a specific coupon, or rate of interest, that does not change for the life of the security. A specific dollar amount will be paid on that bond on an annual basis, and that amount will not change for the life of the bond. A $1,000 bond with a 5% coupon pays $50 per year in interest. If interest rates rise, the only way that this security can be made to yield more and thus be equally attractive to new issues with higher coupons, is to adjust the price downward. Conversely, if rates move lower, the price of the bond would be adjusted higher-to equal current rates (thus more money is required to earn the same $50).

Call Risk. It is common for some types of bond issues to include a provision in the indenture (the contact between the issuer and the bondholder, which sets forth all the terms of the bond and obligations of the issuer) that gives either the bondholder and/or the issuer an option to take some action prior to the stated maturity of the security. The most common type of option embedded in a bond is a "call" feature. This provision grants the issuer the right to retire the debt, fully or partially, before the scheduled maturity date. The issuer usually includes this right in order to have flexibility to refinance the bond in the future if the market interest rate drops below the coupon rate. From the investor's perspective, the disadvantage of call provisions is an inability to project accurate cash flow patterns and an exposure to increased reinvestment risk. The main advantage to purchasing a bond with a call provision is that the investor is compensated for taking a call risk by receiving a higher yield than one would for a duplicate bond without the call feature.

Default Risk. Default risk, also referred to as quality or credit risk, refers to the risk that the issuer of a bond may default, i.e., will be unable to make timely principal and interest payments on the issue. Default risk is gauged by a number of methods, but the most reliable is the quality ratings assigned by commercial rating companies such as Moody's Investor Service, Standard & Poor's Corporation, Duff & Phelps, Fitch Investor Service, as well as the credit research staffs of brokerage firms.

Default occurs when the borrower is unable to repay the obligation. Generally, securities issued by the federal government and its agencies are considered the most secure, while securities issued by private corporations or negotiable certificates of deposit issued by commercial banks have a greater degree of risk. Securities with additional credit enhancements, such as bankers acceptances, collateralized repurchase agreements and collateralized bank deposits are somewhere in-between the two on the risk spectrum. The default risk of the various securities relative to each other is further described below.

Inflation Risk. Inflation risk or purchasing power risk arises because of the variation in the value of cash flows from a security due to inflation, as measured in terms of purchasing power. For example, if investors purchase a bond on which they can realize a rate of return of 7%, but the rate of inflation is 8%, the purchasing power of the cash flow actually has declined such that at the end of ten years, the money earned would be 10% lower than the increase in the cost of living for the same period.

Liquidity Risk. Liquidity of a security refers to its marketability-the quality of an asset that permits it to be converted quickly to cash without a significant loss of value. For an investor who plans to hold the bond until the maturity date, liquidity risk is less of an issue. However, it is important for cash management oriented portfolios that a sufficient portion of the portfolio be invested in securities providing a high degree of liquidity in order to cover any unexpected expenditures.

Evaluating Investment Instruments

Each of the foregoing investment instruments has properties that differentiate it from others in the marketplace. Accordingly, every instrument is likely to carry a yield or price somewhat different from the others. As a group, fixed income instruments generally are considered relatively risk-free investments, and those permitted in the Government Codes for local agencies are believed to be extremely safe securities with minimal chance of default.

Nonetheless, there are still relative differences in the safety or credit risk associated with the various securities, for which measurable yield differentials should be expected.

Treasury securities representing direct issues of the U.S. government are considered risk-free. Due to this risk status, the returns available on Treasury issues tend to be lower than any other securities issued in the U.S.

Closely resembling the safety offered by U.S. Treasury securities are the debt obligations of U.S. government agencies. These are considered exceptionally sound; however, because they do not have direct access to the Treasury, there is a difference in their quality versus Treasury issues. In the past, various factors have reduced the perceived liquidity and default risk of various Federal Agency issues.

Although bank and primary dealer-issued repurchase agreements collateralized by U.S. government securities would seem to occupy the next space on the risk scale investments in agreements that extend beyond a 24 hour horizon reduces the advantage that their liquidity provides, and extended term investments are not recommended.

Banker's Acceptances occupy a lofty niche in the safety scale, possibly equal to Agencies. Collateralized by shipments of goods, and bearing a pledge of credit by the issuing institution as well as the accepting institution, bankers' acceptances have experienced no known defaults in 70 years of trading in the United States.

Certificates of deposit hold a level of safety that improves if compared to Repos with extension. Because they are quite liquid, they are often preferable to repos, though the underlying securities in repos may be of higher quality. Were a bank to fold, depositors normally will be repaid before either debt or equity investors, and negotiable CDs are legally considered deposits. From a practical viewpoint, neither FDIC insurance or collateralization help the depositor gain repayment for amounts above $100,000. Negotiable certificates of deposit are only as secure as the issuing institution behind it. Therefore, quality varies among issuers.

High-grade commercial paper claims the next level of creditworthiness. It should be noted that it is extremely rare for top-graded paper to default while carrying the Al/P 1 rating, although some companies that were top rated have defaulted after ratings were adjusted. In fact, the only corporations rated A1/P1 within weeks of default have been instances associated with court cases, natural disasters, or most recently, in the case of the California utilities, due to an energy supply crisis.

Credit Ratings

Securities expose investors to credit risk. Consequently state law and the County Investment Policy require certain securities to have minimum credit ratings prior to purchase. Rating is the judgment of creditworthiness of an entity or issue made by an accepted rating service. California Government Codes require that commercial paper must have the highest ratings provided by Standard and Poor's or Moody's, which is "A-l/P-l ."

Credit rating agencies use the following considerations to value debt:

- likelihood of default, which is the capacity and willingness of the obligor to make the timely payment of interest and repayment of principal in accordance with the terms of the obligation.

- the nature of and provisions of the obligation.
- protection afforded in the event of bankruptcy, reorganization, or other arrangement under the laws of bankruptcy and other laws affecting creditor's rights.

The five nationally recognized commercial rating companies are Moody's, Standard & Poor's, Thomson Bank Watch, Duff & Phelps, and Fitch Investors Service. The two most widely used systems of short and long-term bond ratings are Moody's and Standard & Poor's, and it is these two that are most often referred to in the Government Codes. Fitch is also recognized for commercial paper and other short term issues and is becoming more accepted in fixed income markets overall. Duff & Phelps ratings are not widely recognized and Thomson rates only banks. Below is a table explaining the short-term ratings of three of these systems.

Short Term/Commercial Paper Investment Grade Ratings			
Rating Interpretations	Moody's	Standard & Poor's	Fitch
Superior Capacity ❑	P1	A1+/A1	F1+F1
Strong Capacity□	P2	A2	F2
Acceptable Capacity □	P3	A3	F3

Mitigating Risk

In light of the recent experience with PG&E commercial paper, the question needs to be asked and answered as to whether there is a flaw in the Policy that allowed an unsafe investment. And, does commercial paper confer more risk than the rewards associated with its higher return justify? What are the risks and what are the rewards?

Risks of Purchasing Commercial Paper. As discussed above, commercial paper is unsecured and the bankruptcy of the issuing company will leave the holders of the commercial paper standing in line behind the secured creditors and most senior debt holders. State law and the County's Investment Policy limit the purchase of commercial paper to only those that are rated at least A-l/P-l, and limits the Investment Pool's holdings in commercial paper to 40% of the total investible funds. Over the past 30 years, no firm rated A-l/P-l at the time of purchase has failed to repay their debt. The County's Investment Policy also limits risks in this category by requiring diversification and by requiring that such investments be short term.

Reward of Purchasing Commercial Paper. During the course of a year the yield on 90 day commercial paper is usually 1 to 2 percent above other 90 day issuances, such as Treasuries. Assuming the County's portfolio to be $500,000,000, and the commercial paper holdings to be 40% of the total investible funds, this difference in yield can amount to $2,000,000 - $4,000,000 on an annual basis. It appears to be the consensus of the State Legislature and the State Treasurer, and each County Treasurer in the State that the reward offered by additional interest earned in these investments is not outweighed by the potential risk.

Anatomy of a Trade – The Investment Process

When an investment needs to be made it is the practice of the County Treasurer's Office to first obtain various reports that indicate: 1) existing investments and their maturity dates; 2) the percentage of room in each type of security for additional investments in that category, based on the provisions of the Investment Policy, and 3) where investments should be made to cover known expenditures.

On the morning of a trade, the investment officer consults with the County's paid investment advisor. This discussion covers what is happening in the market, including changes in the yield curve and the types of securities available that seem to offer the best return versus risk, and whether the investment is best kept short or extended.

Following this discussion, and per the Investment Policy, the investment officer contacts at least three brokers to obtain quotes for various securities. Prior to the actual buy, the investment officer may again confer with the investment advisor as to the options available and receives his input as to the choices. At this time, the advisor will often also provide information on other potential investments that he may be aware of through his Wall Street sources. It is normal for a consensus to be arrived at prior to the investment officer making the final decision, though on some occasions it may be that the investment officer will make an investment after only the preliminary discussion.

Reporting and Oversight

Prior to the legislation that resulted from the Orange County debacle, the primary Treasurer's report to the Board of Supervisors was the Monthly Treasurer's Report, which provides for an accounting of cash on hand and interest earned. The Monthly Treasurer's report did not provide all aspects of the status of investments in the County's Investment Pool or enhance the understanding of the Treasurer's actions. It required only an accept and file action by the Board of Supervisors, and as such, provided an official record that met the needs of the Auditor and other parties. Legislation enacted after the Orange County financial crisis provided the Board of Supervisors an opportunity for input to and review of the Investment Policy on at least an annual basis, provides for a detailed report on the County's investments on a quarterly basis, provides for a Treasury Oversight Commission to provide additional public input and oversight to the County's investment goals and processes, and provides for an annual audit.

Recommendations

The investment in PG&E commercial paper was made within all known and accepted guidelines for preventing the loss of investment principal, and within the guidelines provided by the County's Investment Policy. It is believed that no corrections or adjustments to the Investment Policy can guarantee that a similar problem would not occur in the future. However, our office can assure the County Board of Supervisors and members of the public that as much as is possible and practical, each and every issuer and each investment option will be reviewed thoroughly before any security is purchased, and consistent with existing procedures and the Auditor's recommendation, the County's investment officer will consult with the County's financial advisor prior to making the decision to invest in specific issues of commercial paper.

COUNTY OF SANTA CRUZ

PROPOSED

2001
INVESTMENT POLICY

County of Santa Cruz
STATEMENT OF INVESTMENT POLICY

Under the laws of the State of California, it is the responsibility of the County Treasurer, at the direction of the Board of Supervisors, to secure and protect the public funds of the County and the participants of the Investment Pool, and to establish proper safeguards, controls, and procedures to maintain these funds in a lawful, rational and auspicious manner. Said maintenance shall include the prudent and secure investment of those funds that are deemed temporarily excess, in a manner anticipated to provide additional benefit to the people of the County of Santa Cruz. In addition, the County Treasurer acts as the Treasurer, cash manager, and investor for a sizable number of public agencies within the County rather than each entity having to locate and hire a knowledgeable person to handle the entity's banking, investments, and other financial duties separately. This pooling of public funds eliminates duplication of expenses, smooths out cash flow, permits cost savings through higher volume, and attracts more professional service providers.

This Statement of Investment Policy will be provided annually for the review of the Treasury Oversight Commission and the approval of the Board of Supervisors in an open public meeting.

SCOPE

This Statement of Investment Policy pertains to those temporarily excess funds under the control of the Treasurer, designated for the daily ongoing operations of the County and pool participants; and concerns the deposit, maintenance, and safekeeping of all such funds, and the investments made with these funds. This Policy does not apply to pension moneys, deferred compensation funds, trustee, and certain other non-operating funds not participating in the County Investment Pool.

PURPOSE OF POLICY STATEMENT

The purpose of this Statement of Investment Policy is to provide the Board of Supervisors, the Treasury Oversight Commission, those entities invested in the County Investment Pool, those involved in servicing the investment requirements of the County, and any other interested party, a clear understanding of the regulations and internal guidelines that will be observed in maintaining and investing those pooled funds deemed temporarily excess.

TREASURY OBJECTIVES

The underlying objective of the Treasurer is to protect the safety of the principal of the County Investment Pool through the judicious purchase of those legal investments permitted to local agencies, as defined in the State of California Government Codes, consistent with current conditions and the other dominant objectives pursuant to managing a local agency portfolio, namely:

Safety: It is the primary responsibility of the Treasurer to maintain the safe return of all principal placed in investments by avoiding decisions that might result in losses through either fraud, default, or adverse market conditions. Import is also accorded the protection of accrued interest earned on any investment instrument.

Liquidity: It is imperative that a vast majority of all investments be in items that are immediately negotiable, as the portfolio is a cash management fund. It shall always be assumed that all investments could require immediate liquidation in order to meet unexpected cash calls.

Availability: Due to the nature of a public funds portfolio, it is mandatory that moneys be available to meet the monetary requirements inherent to operating a public entity. Thus funds need to be invested in such a manner that money will always be available to pay normal cash requirements. A sufficient portion of all funds shall be invested in securities providing a high degree of liquidity and availability, that is, in securities easily sold or converted to cash in a timely manner, with little or no loss of interest earnings.

Yield: While it is considered desirable to obtain a respectable yield, yield shall not be the driving force in determining which investments are to be selected for purchase. Yield is definitely considered to be of much lessor importance than either safety, liquidity or availability.

The Treasurer places investments with the objective of obtaining a respectable rate of return, not attempting to maximize yield at the expense of either safety, liquidity, or availability, yet not totally ignoring those factors within the marketplace that may be indicative of either favorable or hazardous conditions. The portfolio will be managed very conservatively, but actively enough to avert avoidable losses due to adverse market conditions.

PRUDENCE

The Treasurer is subject to the "Prudent Person Rule" whenever making a decision regarding the investment of the County's funds. This rule states in principle:

> *"In investing property for the benefit of others, a trustee shall exercise the judgement and care, under circumstances then prevailing, that persons of prudence, discretion and intelligence, would exercise in the management of their own affairs - not in regard to speculation, but in regard to the permanent disposition of their funds considering the probable safety of, as well as the probable income from, their capital."*

The Treasurer, and those acting for the Treasurer, are considered to have a fiduciary, trustee, relationship with the public for the public funds, and all investment decisions will be made in a manner sustaining this responsibility.

DELEGATION OF AUTHORITY

In accordance with Government Code section 27000.1 and County of Santa Cruz Ordinance 4434, the County Treasurer has been delegated the authority to invest and reinvest the funds of the County and the funds of other depositors in the County Pool.

While the Treasurer has final responsibility for all investment decisions, other Treasury personnel may aid in the day to day operations. Those staff members, in addition to the Treasurer, currently authorized to act on behalf of the County, as of the date entered on this Policy, are listed below. This list is subject to change, and those parties involved in transactions with the Treasurer's department should always obtain a current Trading Authorization and Agreement form, and be verbally introduced by a known Treasury employee, prior to accepting unconfirmed verbal instructions from any previously unknown Treasury staff member.

Authorized Personnel	Title
Richard W. Bedal	County Treasurer-Tax Collector
Deborah Lauchner	Assistant Treasurer-Tax Collector
Minerva Torres	Senior Account Technician
Lois Meeker	Senior Account Clerk

Other persons, both inside and outside County employment, may act in the role of assistant or advisor to aid in the timely and proper settlement of investment transactions. While these persons may provide information or aid in the expedient delivery of securities, they may not authorize, approve, or initiate any trading activities. **Only the persons listed on a current *Trading Authorization and Agreement*, and the Treasurer, may initiate trading activity.**

SECURITIES CUSTODY

The Treasurer has established a third party custody and safekeeping account to which all negotiable instruments shall be delivered upon purchase on a payment versus delivery basis. No negotiable, deliverable, securities or investments will be left in the custody of any brokerage firm or issuing party, including any collateral from Repurchase Agreements.

DESIGNATED SERVICE BANK

The Treasurer shall designate a State or Federally chartered bank operating within the State of California to serve as the County's Primary Service Bank, and the Treasury shall use said bank as a clearing house for all funds.

AUTHORIZED INVESTMENTS AND LIMITATIONS

The Government Codes of the State of California, primarily within sections 53600 et. seq., establish the legality of certain types of investment vehicles for a California local agency's portfolio. Thereby, under no circumstances is the Treasurer permitted to purchase an investment that is not specifically authorized for a local agency under these, or other code sections that may apply, or might later be enacted, pertaining to local agency investments. Investment professionals dealing with the County should possess a complete understanding of these Code sections.

An attached Exhibit A briefly describes the types of securities that are legal within the Government Code sections noted above and outlines the various limitations included in these sections. Excepting the restrictions noted below in this section, all legally permitted investment options described in the Government Code are authorized at this time. Funds placed in the State's Local Agency Investment Fund (LAIF) shall follow the limitations placed on these deposits by the State and may change in accordance with these restrictions.

Though these Government Code sections define the investment types and terms permissible to the Treasurer, **the Treasurer will not:**

- Invest in any security or investment with a stated or potential final maturity longer than five years, unless it contains a non-retractable 'put' exercisable within five years. In other words, such a security cannot be purchased by the Treasurer unless it permits the investor the unrestricted choice of selling the security back to the issuer at par, or above, at a time prior to five years.

- Invest in any security or investment wherein interest might not be earned during any period the security or investment exists.

- Purchase floating rate securities containing an inherent yield structure that could dictate a return substantially below rates available for similar maturity periods on the dates the coupon changes.

- Enter into a reverse repurchase agreement.

- Purchase any Collateralized Mortgage Obligations.

- Lend securities.
- Invest in futures or options.

In addition to the limitations provided in State law and this Investment Policy, various temporary and more restrictive constraints may at times be beneficial due to transient conditions within the marketplace. These flexible constraints are not part of this Policy but are presented in a document prepared by the Treasurer entitled "Temporary Constraints and Restrictions on Investments", and will change on an "as needed" basis. The attached Exhibit B is the "Temporary Constraints and Restrictions on Investments" that were in effect when the Board of Supervisors approved this policy. When these constraints and restrictions change, a copy will be immediately sent to members of the Treasury Oversight Commission and the Board of Supervisors. These constraints or restrictions may only be more restrictive than those of the Policy, but may ***not*** be less restrictive. Investment professionals should be aware of these temporary conditions in order to save time and best serve the County.

AUTHORIZED DEALER LIST

It is prohibited for a transaction to be entered into with any securities broker, dealer or bank investment department or subsidiary prior to that entity being designated an Authorized Dealer, and placed on the Authorized Dealer List. For a firm to become authorized it must first demonstrate that it will add value to the Treasurer's efforts to best manage the cash portfolio, as well as fulfill certain other minimum requirements. To qualify for Authorized Dealer status, a brokerage firm or bank must:

1) Be a dealer operation properly licensed to deal with local agencies in California **and;**

2) Have a minimum of $50mm in capital, or, be a Primary Dealer of the Federal Reserve Bank of New York; **and;**

3) Be headquartered in the State of California, or, the City of New York, or be the direct issuer of a security type normally purchased by the Treasurer;
Or;
Be a department or subsidiary of an insured bank with minimum assets of $500mm that the County has comprehensive banking relationships with. Or;

Be a broker operation properly licensed to deal with local agencies in California that has capital of <u>not less than</u> $5mm, that is not directly involved in the actual custody, and transfer of money or securities purchased or sold by the County, but that represents established accounts opened in the County name at those firms meeting the requirements of 1) through

3) of this section, wherein all dealings would be the responsibility of the dealer operation, and wherein all deliveries, payments, written confirmation, etc. will originate with the qualified dealer operation and are sent directly to the County.

If meeting the above requirements, a salesperson may apply to become an Authorized Dealer by sending to the Treasurer their most recent annual and interim audited financial statements and a letter furnishing:

1) Their reasons for believing they would add value to the present coverage; **and,**

2) A general roster of those markets they participate in, and specifics on those types of securities they as a firm, regularly issue or regularly hold dealer trading positions in; **and,**

3) A list of **five** references, at least three being California local agency treasurers, including telephone numbers, that the Treasurer or his representative may contact.

The Treasurer will instigate an investigation of the applying salesperson and the firm through various sources, including the California Department of Corporations and the National Association of Securities Dealers (N.A.S.D.), to determine market participation, knowledge, reputation, and financial stability. All salespeople and their supervisors will be expected to have a working knowledge of the appropriate sections of the State of California Government Code, sufficient experience in covering public entities, a willingness to well serve their customers, a complete and total understanding of this Investment Policy, and demonstrate an ongoing ability to work with the Treasurer and staff. The Treasurer will review all new requests at the end of each quarter, and if the decision is made that additional dealers would be beneficial to best service the portfolio's needs, those dealers selected will be informed of their addition to the Authorized Dealer List. All dealers are subject to removal from the Authorized Dealer List at any time, solely at the discretion of the Treasurer.

The Treasurer, or Treasury staff, are prohibited from dealing with a salesperson, broker, or account executive from any broker, dealer or bank investment department or subsidiary until the Acknowledgment form found on the last page of the *Trading Authorization and Agreement* is signed by all parties and received by the Treasurer. The *Trading and Authorization Agreement* is sent to all approved dealers and is an integral part of this Policy Statement for Brokers/Dealers, etc. doing investment business with the County Treasurer or Treasury staff.

Similar restrictions and forms may be required of those firms doing business with the County through retained financial advisors or managers. Certain selected firms may be chosen or appointed by the Treasurer to render specific services the Treasurer determines they are uniquely qualified to provide, wherein some of the requirements of this section may be waived.

Neither the Treasurer, nor any member of the Treasurer's staff, may accept any gift, honoraria, gratuity or service of value in violation of the regulations set forth by the Fair Political Practices Commission, the Government Codes, additional limitations set forth by County ordinance, or internal requirements of the Treasurer. The Treasurer and all members of the Treasury staff are prohibited from conducting any business with any broker, dealer, or securities firm that has made a political contribution within any consecutive 48 month period beginning January 1, 1996, in an amount exceeding the limitation contained in Rule G37 of the Municipal Securities Rulemaking Board, to the County Treasurer or any member of the Board of Supervisors, or any candidate for these offices.

THE COUNTY TREASURY OVERSIGHT COMMISSION

In accordance with Government Code section 27130 et seq. and County Ordinance 4433, there shall be a Treasury Oversight Commission of five members appointed from the following:

a) An appointed representative of the Board of Supervisors.
b) The County Superintendent of Schools, or designee.
c) A representative selected by a majority of the presiding officers of the governing bodies of the school districts and community college districts of the County.
d) A representative selected by a majority of the presiding officers of the legislative bodies of the special districts within the County that are required or authorized to deposit money in the County Investment Pool.
e) A public member who shall have expertise in, or an academic background in, public finance.

Restriction of Members - All members of the Treasury Oversight Commission are restricted as follows:

- A member may not be employed by an entity that has (a) contributed to the campaign of a candidate for the office of local treasurer; or (b) contributed to the campaign of a candidate to be a member of a legislative body of any local agency that has deposited funds in the county treasury, in the previous three years or during the period that the employee is a member of the commission.
- A member may not directly or indirectly raise money for a candidate for local treasurer or a member of the governing board of any local agency that has deposited funds in the county treasury while a member of the commission.
- A member may not secure employment with bond underwriters, bond counsel, security brokerages or dealers, or with financial services firms during the period that the person is a member of the commission or for three years after leaving the commission.
- Members may not receive honoraria, gifts, gratuities or service of value from advisors, brokers, dealers, bankers, or other persons with whom the county treasury conducts business.

The Treasurer will annually provide a copy of the Investment Policy for review and monitoring by the Treasury Oversight Commission. The Treasurer will provide a report quarterly to the Board of Supervisors and the Treasury Oversight Commission, identifying all investments held in the County Investment Pool, or elsewhere by the Treasurer. The Treasury Oversight Commission shall, via this report and other appropriate means, monitor the activities of the Treasurer, and cause to be performed an annual audit to determine the Treasurer's compliance with this Investment Policy, and other appropriate regulations.

Commission meetings shall be open to the public and in compliance with the appropriate sections of the Ralph M. Brown Act. By Code, all costs related to the duties of the Treasury Oversight Commission will be considered normal charges against earnings of the Investment Pool.

The Treasury Oversight Commission shall have no authority to direct the process or daily operation of any portion of the Treasury department, nor shall the Commission play any role in determining which banks, firms, or individuals the Treasurer does business with, nor shall the Commission be involved in determining which investments the Treasurer purchases, but shall act only to review the actions of the Treasurer to determine that they are in accordance with the Investment Policy and all other legal requirements or regulations.

TERMS FOR FUNDS INVESTED WITH THE COUNTY INVESTMENT POOL

The Government Code requires the County Treasurer to define the limits and conditions under which local agencies having their money in the Investment Pool may deposit and withdraw their funds. The Government Codes confer upon the Treasurer the final authority as to how funds for which the Treasurer is held responsible for overseeing, are to be invested. The Treasurer must take into account the current financial condition of the sum total of the Pools' agencies, the conditions of the market place, as well as the cash flow projections and the potential for changes in the Pool's cash needs. The Treasurer must protect the earnings of each individual local agency in the Pool, and also see that no decision will reward a particular agency or group of agencies within the Pool at the expense of another or others within the Pool. If the Treasurer determines that a request for a withdrawal of funds for a specific or outside investment is not, in the Treasurer's opinion, in the best interest of a particular agency, or is overly detrimental to the Pool as a whole, the Treasurer must legally deny the request, or find a means of neutralizing the harm to all those affected.

FUNDS OF AGENCIES REQUIRED TO INVEST WITHIN THE POOL

Funds will be accepted at all times, in the manner prescribed, from those local agencies where the County Treasurer is also the Treasurer for the local agency, or from any agencies that by statute must place their money in the County Investment Pool. Funds will earn interest based on the average daily balance distributed on a monthly basis.

Should a legislative body of a local agency determine that certain funds will not be required by the local agency for a period of at least one year, the local agency may petition the County Treasurer to invest that portion of the local agency's excess funds in a specific investment under the control of the County Treasurer. Such a petition should state the nature of the funds the legislative body wishes to invest specifically, and the reasons why the legislative body believes a specific investment is a preferable and viable alternative to the general Pool participation. Should the Treasurer determine that the request for a specific investment is valid and not overly counter-productive to the Pool as a whole, the Treasurer will consult with the local agency's legislative body, or its appointed representative, to suggest and determine exactly what investment(s) should be purchased to fulfill the needs of the local agency. The Treasurer will then purchase the specific investment(s) upon receipt of a written resolution, issued by the legislative body of the local agency, requesting the specific investment. The resolution must acknowledge that the local agency's legislative body takes full responsibility for the decision to purchase the specific investment(s), and that should conditions change requiring a sale prior to maturity of the specific investment(s), any loss that might be suffered as a result, will be solely that of the local agency, and that this loss shall not be shared by the Pool as a whole, nor by the County.

Under language added to the Government Code in 1995, it is not permissible for local agency legislative bodies, required to have their funds within the Pool, to withdraw funds from the Pool in order to invest outside the County Pool in any manner, at any time without specific permission of the Treasurer. Any such investments shall be either terminated and all funds returned to the Pool, or the securities so purchased must be transferred to the custody of the County Treasurer immediately. Upon receipt of any such securities by the Treasurer, the Treasurer shall at the Treasurer's option, place the investment in the Pool, terminate the investment at the current market value and credit the local agency with the proceeds, or place the security in the name of the local agency as a specific investment.

MONEY VOLUNTARILY INVESTED WITH THE COUNTY INVESTMENT POOL

By Code, the County Treasurer shall limit the amounts and set conditions under which money from local agencies, not required to have their funds in the Investment Pool, may deposit and withdraw voluntarily invested funds. Local agencies from outside the County will not be permitted to deposit funds in the County Pool. Funds from local agencies within the County, voluntarily wishing to participate in the Pool, will not be accepted under normal conditions unless the Treasurer is assured that these funds are in lieu of longer term investments. Such deposits are subject to withdrawal restrictions for a set minimal term as to be agreed to, prior to the funds being accepted into the Pool, and may not be withdrawn at any time without a minimum of thirty days notice of "intent to withdraw."

Under normal conditions, voluntary money withdrawn from the Pool will be disbursed on a dollar for dollar basis, plus appropriate interest, but under adverse market conditions, when the Treasurer deems the withdrawal of voluntary funds would cause undue losses or significantly lower earnings for those local agencies remaining within the Pool, the Treasurer may require one or more of three remedies:

1) restrict the percentage of funds that may be withdrawn in any given month 2) restrict the rate at which the funds may be withdrawn, or 3) require the local agency withdrawing their funds to accept their funds based on the current market value of the overall Pool.

These terms will be agreed to and contracts signed prior to any voluntary money being accepted into the County Investment Pool. Such terms may exceed minimum requirements set forth in the Government Codes.

Specific investments are not normally permitted with voluntary funds, though on a cost recovery basis and under circumstances that dictate such activity, exceptions may be permitted.

POOLING FUNDS AND DISTRIBUTING EARNINGS

Funds available from all sources may be pooled in order to achieve greater investment potential. The earnings from the pooled investments shall be deposited in a special fund. Each month the Earnings Fund will be shared and each participant in the Pool will be credited with interest proportional to the size of their investment, based on the average daily balance.

Funds placed in specific investments earn the yield of the investment, not the return earned by the Pool. Earnings on specific investments will be distributed within thirty days of receipt.

CALCULATING AND APPORTIONING COSTS

The County Treasurer, following the criteria outlined by the Federal Office of Management and Budget circular #A-87, will determine the “administrative cost” of investing or handling of funds as well as the cost of equipment which expedites processing. This cost shall be deducted prior to interest apportionment and shall be shared proportionately by all pooled and specific investments.

REPORTING

The Treasurer will report to the Board of Supervisors and the Treasury Oversight Commission on a quarterly basis the holdings, status, and earnings of the portfolio. The Statement of Investment Policy will provide annually for the approval of the Board of Supervisors and for review by the Treasury Oversight Commission. Should circumstances require revision within this Policy during the year, the changes will be presented to the Treasury Oversight Commission, and approval obtained from the Board of Supervisors prior to these alterations being adopted.

Exhibit A
Investments Allowed by State Law

Investment Type	Maximum % of TIF*	Maximum Maturity	Quality Requirements
a. Bonds issued by a local agency	100%	None	None
b. Treasury Obligations	100%	None	None
c. State of California Obligations	100%	None	None
d. Obligation of Calif local agency	100%	None	None
e. Obligations issued by Federal Agencies, and U.S. and Government sponsored enterprises	100%	None	None
f. Bankers Acceptances	40%	270 days	None
g. Commercial Paper	40% max. 10% of portfolio per issuer max. 10% of issuer's program	180 days	U.S. Corporations with $500MM in assets, A or higher rating for issuer's debt, by Moody's and S&P
h. Negotiable C.D.s	30%	5 years	None
i. Repurchase Agreements	100%	1 year	Collateral must be a legal investment
j. Reverse Repurchase Agreement	20% of base	92 days maximum, or to maturity	Collateral must be a legal investment
k. Medium Term Note	30%	5 years	U.S. Corporations, or Banks licensed within any State of the U.S., "A" or better rating by major rating service
1. Mutual Funds	20%, 10% per fund	NA	A defined money market fund; or invest only in a-j, m, n of this list, as restricted; highest letter and number ranking of 2 of 3 rating services; or a SEC Registered Advisor with 5 years.
m. Investments as permitted by provision in agreements of indebtedness	As per bond agreement	NA	Not contrary to 53635 and other pertinent law
n. Asset secured indebtedness	100%	None	As required by 53652
o. Collaterallized Mortgaged Obligations	20%	5 years	issuer must be rated "A" minimum, security must be "AA" by national rating service
p. Contracted Non-neg Time Deposits	100%	None	None--% of asset limits

*Total Investible Funds (TIF)-for purposes of this Policy, are all funds in the Pool that are available for investment at any one time.

Temporary Constraints and Restrictions on Investments

a. **Bonds issued by the County or County Agencies.** The Treasurer may purchase debt issued by the County or its agencies, but any such debt purchased will normally be obtained only directly from the issuing agency and not in the secondary market. Such issues, along with issues from 'c' and 'd' below, shall not exceed 10% of the total portfolio.

b. **U.S. Treasury obligations.** The Treasurer will attempt to purchase U.S. Treasury obligations for the liquidity and availability they provide when investing in issues beyond two years. However, the spread available on issues with less availability or quality may suggest that other issues be substituted. Treasury issues will not be limited in quantity, though the cash flow requirements of the Pool shall be considered when purchasing longer term maturities.

c. State of California Obligations. The Treasurer does not currently invest in State obligations, though participation in the Local Agency Investment Fund is part of the overall investment strategy, and the holding of interest bearing State issued warrants as an investment alternative is permissible under some occasions. State issued obligations, with the exception of LAIF investments, along with issues from 'a' and 'd', shall not exceed 10% of the overall portfolio.

d. **Obligations of another California local agency.** The Treasurer does not currently purchase these securities due to tax considerations, but may purchase taxable issues. The total of such issues, along with issues from 'a' and 'c' above, shall not exceed 10% of the overall portfolio. Tht total of all such individual local agency issues, along with issues from 'a' to 'c' above, shall not exceed 10% of the overall portfolio. LAIF investments shall not be included when calculating this percentage, nor shall investments in joint power authorities that resemble money market mutual funds such as CAMP and CLASS. Maximum investments in LAIF shall be governed by the maximum permitted by the State. Investments in joint powers authority investment funds shall not exceed 25% of the Pool's include specific investments or individual local agency's investments of bond proceeds not made through the Pool.

e. Obligations of the various Federal Agencies. The Treasurer currently does not invest in any long term pooled securities issued by GNMA, FHLMC, SBA, or any Federal agency with a maturity based on average life calculations. Due to the frequent concerns for the safety and liquidity levels of many agency obligations, the Treasurer monitors and may restrict the purchase of any particular agency's securities at any time. Agency obligations are expected to yield a reasonable spread over Treasury issues of the same maturity, and the Treasurer will generally not purchase any agency obligations for a spread below a minimum of 10 basis points. No single agency will account for more that 15% of the portfolio at this time, nor will the total of all Federal agencies exceed 40% of the portfolio.

f. **Bankers Acceptance.** The Treasurer currently purchases B.A.s from those banks ranked in the top 100 world banks or the top 20 U.S. Banks on the latest compilation by the American Bankers Association. Foreign banks shall be headquartered in certain Western European countries, Canada, or Japan. For additional potential restrictions see section 'p' below.

g. **Commercial Paper.** The Treasurer currently does not allow the percent of commercial paper to exceed 30% of the total portfolio unless the weighted average maturity of commercial paper is under 60 days. See section 'p' below for additional restrictions on particular Commercial Paper issues.

h. **Negotiable Certificated of Deposit.** The Treasurer currently purchases those types of Negotiable C.D.s permitted by the Government Codes, from certain banks listed in the top 100 world banks or the top 20 U.S. banks, as registered in the most recent American Bankers Association compilation, that also receive a long term debt rating of "A" or better by S&P and Moody's, and a short term rating of investment grade. Additionally, the Treasurer monitors, and therefore may possibly eliminate those banks whose marketability and liquidity may be considered suspect due to their pricing within the secondary markets. Negotiable S&L and savings bank C.D.s are not currently purchased. The Treasurer currently is not purchasing fixed rate C.D.s with a maturity beyond two years nor any type of C.D. with a maturity beyond five years. Any C.D.s purchased with a maturity longer than one year may pay interest no less frequently than semiannually. Please see section 'p' below for additional restrictions on C.D. purchases.

I. [a] **Repurchase Agreements.** Repurchase agreements will only be entered into with Primary Dealers, and all collateral will be delivered to a third party designated by the Treasurer, as per state law. Due bills are not acceptable, nor, except in cases of extreme emergency, are substitutions of collateral on agreements under thirty days. The Treasurer will constantly monitor the market value of all collateral and shall require additional collateral if the market value falls to a level of 100% of the cash value invested, when Treasury Notes and Bonds are the collateral, and at higher levels for other types of collateral. Treasury Notes and Bonds will be collateralized at a minimum of 102% of market at the start of the repo, for short term repos, and possibly at higher levels for longer term repos, (percentage determined by market conditions, etc.). Repo agreements with Treasury Bills or other discounted securities as collateral will be priced to market and collateralized at a minimum of 102% of market, (actual percentage to be determined by collateral type, conditions, etc.). Collateral with maturities beyond five years are not acceptable, (except in certain limited cases where unrestricted 'puts' are included with the issue), and all collateral must meet the same requirements as purchased securities. Repurchase Agreements will not be entered into for periods longer than ninety days. Repurchase Agreement contracts will be on file for any dealer with which the County does Repos. See section 'p' below for other potential restrictions on Repo collateral.

[b] **Reverse Repurchase Agreements.** The County Investment Policy does not allow the Treasurer to enter into Reverse Repurchase Agreements.

j. **Medium Term Notes.** The Treasurer currently purchases Medium Term Notes with a rating of "A" or better for a maturity of up to one year. Maturities beyond one year requires a rating of "AA" or better. See section 'p' below for additional potential restrictions on Medium Term Notes.

k. **Mutual Funds.** The Treasurer currently imposes no additional restrictions on Mutual Fund purchases beyond those in the Codes.

1. **Investment of Bond indebtedness.** The Treasurer will consider GICs and other issues as bond documentation permits.

m. **Asset backed securities.** The Treasurer buys only asset backed commercial paper with maturities under 180 days.

n. **CMO investments.** The County Investment Policy does not allow the Treasurer to purchase any Collateralized Mortgage Investments.

o. Contracted Non-negotiable Time Deposits. The Treasurer will enter into contracts for Time Deposits of amounts greater than $98,000, only with those banks that meet the requirements for investment in Negotiable C.D.s, or with those banks headquartered or with a branch within the County, that are rated "A" or better by Gerry Findley Inc. or an equivalent rating of a similar agency. Time Deposits for amounts of $98,000 or less shall be with California institutions rated "A" or better by Gerry Findley Inc. or a similar rate and rating agency, having assets of at least $25,000,000 and shall require at least quarterly interest payments. Issuers of all Time Deposits shall agree to early withdrawal, under a bona fide emergency circumstance, with penalties not exceeding an interest adjustment to the level of the yield available to the investor on the original settlement date, for the shorter time period actually held. The maximum maturity on any Time Deposit shall usually not exceed 6 months, nor shall the total of all Time Deposits exceed 10% of the total portfolio. Mandated deposits or investments specifically invested by pool participant's request are not included in this percentage restriction. See section 'p' below for additional potential restrictions.

p. **Exposure Limits.** Presently the total exposure to any one issuer, when totaling all types of securities shall not exceed 10% of the total portfolio on date of purchase. Possible exceptions to this rule shall include U.S. Treasury issues, Federal Agency issues, local agency issues, and funds in LAIF. Repurchase Agreement collateral shall not be excluded from this calculation unless the Repurchase Agreement is for 5 business days or less. Exposure to the overall credit of individual foreign countries shall be monitored and maintained at prudent levels. ~~Under generally accepted practices, exposure limits are calculable on the purchase date of the investment only.~~

q. **Lending Securities.** The County Investment Policy does not allow the County Treasurer to lend securities.

r. **Futures and Options.** The County Investment Policy does not allow the Treasurer to invest in futures or options.

s. Maturities over one year. Any investment made with a maturity exceeding two years shall require prior written approval of the Treasurer. The Treasurer may provide temporary exemptions for specific employees for a period not to exceed one year such that each individual investment shall not require specific approval.

t. State law states that all reauired percentages included within investment related sections of the Government Codes are only binding: on the day the investment is made. and that future changes in the size of the portfolio do not require the Treasurer to readjust the total percentage of each securi type within the uortfolio to reflect the change in size. Neither is it necessary to sell an investment when changes occur such that the security no longer meets the minimum reauirements of the Codes. or the Codes are changed such as to no longer include certain current holdings. The Treasurer shall weieh the change in risk and determine whether or not a security should be sold within the portfolio after a change in conditions or the Codes result in a particular security no longer meeting existing or new regulations.