



**SAN DIEGO COUNTY
REGIONAL AIRPORT AUTHORITY
EXECUTIVE COMMITTEE**

Item No.

4

Meeting Date: **MAY 23, 2011**

Subject:

Annual Review and Update of Authority Policy 4.20 – Guidelines for Prudent Investments, and Delegation of Authority to Invest and Manage Authority Funds to the Vice President, Finance/Treasurer

Recommendation:

Forward this item to the Board for approval.

Background/Justification:

The investment policy (Attachment A) serves as the foundation of the Authority's investment goals and priorities. The Authority's Internal Policy Guidelines compels the Authority's Treasurer to invest Authority funds in a manner that will provide the highest security of funds while meeting the daily cash flow demands. The foremost stated objective is safety, with the requirement that all transactions are structured to avoid capital losses from issuer or broker/dealer default, or erosion of market value.

State law requires that the objective of return on investment be subordinate to the objectives of safety and liquidity. Therefore, the investment policy requires the Authority to achieve a return on funds throughout all economic cycles, taking into consideration the Authority's investment risk constraints and cash flow requirements.

The Authority's Investment Policy was developed in conjunction with our financial and investment advisors and it adheres to and exceeds the policies and requirements of investment types as authorized by the California Government Code Section 53600 et seq ("Code").

The recommended changes to the policy include language that specifies that market value shall be used to calculate portfolio limits, further clarification on portfolio percentage limits for certain types of certificates of deposit, the addition of Long Term Notes (LTNs) with less than 5 years until maturity as an allowable investment, additional language to establish procedures for Local Government Investment Pools investment policy compliance, adding negotiable certificates of deposit to the list of securities that require safekeeping by a third party, revised internal control language to indicate the Treasurer's responsibility to review and present performance standards, and updated the Glossary of Terms.

Section 53646(a) of the Code states that the treasurer or chief fiscal officer of any local agency may annually render to their legislative body and any oversight committee an investment policy, which the legislative body shall adopt at a public meeting.

While an annual review and adoption is not required by statute, both the Association of Public Treasurers of the United States and Canada and the Government Finance Officers Association have established policy standards recommending a review be conducted annually.

Since this policy serves as the guidelines for prudent management of our investments, the attached resolution and accompanying policy are submitted to ensure a regular review and approval by the Authority Board.

In addition, the Board delegates the authority to invest and manage the funds of the Authority to the Authority's Treasurer. Such delegation is on a fiscal year basis and subject to renewal by the Board, at its option. Based on the investment record, the attached resolution requests reappointment of the Vice President of Finance/Treasurer to continue this role for another year.

The existence of an approved investment policy demonstrates that the Authority Board and staff are fiducially responsible; thereby, promoting trust and confidence from the public that it serves. This annual review is done to ensure the Authority Board's continued oversight and approval of the policies, rules, and performance regarding the investment of Authority funds.

This review also will result in the reappointment of the Vice President of Finance/Treasurer with the authority to continue investing and managing the Authority's funds.

Fiscal Impact:

None.

Environmental Review:

- A. This Board action, as an administrative action, is not a project that would have a significant effect on the environment as defined by the California Environmental Quality Act ("CEQA"), as amended. 14 Cal. Code Regs. §15378. This Board action is not a "project" subject to CEQA. Pub. Res. Code §21065.
- B. California Coastal Act Review: This Board action is not a "development" as defined by the California Coastal Act Pub. Res. Code Section 30106.

Equal Opportunity Program:

Not applicable.

Prepared by:

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VICE PRESIDENT, FINANCE/CHIEF FINANCIAL OFFICER/TREASURER

SAN DIEGO COUNTY REGIONAL AIRPORT AUTHORITY
POLICIES

ARTICLE 4 - FINANCE AND ACCOUNTING
PART 4.2 - INVESTMENTS
SECTION 4.20 - POLICY GUIDELINES FOR PRUDENT INVESTMENTS

PURPOSE: To establish a policy governing the investment policies and practices of the San Diego County Regional Airport Authority (the “**Authority**”), including risk management.

POLICY STATEMENT:

It is the policy of the Authority to invest public funds in a manner that will provide the highest security of the funds under management while meeting the daily cash flow demands of the Authority. The investment policies and practices of the Authority are based upon prudent money management and conform to all state and local statutes governing the investment of public funds.

This policy also addresses risk management because risk management is an integral part of managing a fixed income portfolio. To focus only on maximizing return is imprudent; therefore, policy issues will be directed to limiting the investment portfolio’s exposure to each issue and issuer of debt and criteria for establishing minimum credit requirements that firms must have in order to effect security transactions with the Authority.

(1) Scope. This investment policy applies to all the Authority’s investment activities, except for the Employees Retirement and Deferred Compensation funds, which are administered separately. In addition, in the event of a conflict between this policy and permitted investments of bond proceeds as defined by a master indenture or supplemental indenture (“**Indenture**”) associated with any Authority debt issuance, this Policy shall control. The financial assets of all other Authority funds shall also be administered in accordance with the provisions of this policy.

(2) Objectives.

(a) Safety of Principal. Safety of principal is the Authority’s foremost objective. To accomplish this objective, diversification is required in order that potential losses on individual securities do not exceed the income generated from the remainder of the portfolio. Each investment transaction shall seek to ensure that capital losses are avoided, whether from issuer default, broker/dealer default or erosion of market value. The Authority shall seek to preserve principal by mitigating credit risk and market risk.

(i) Credit risk is the risk of loss due to failure of the issuer to repay an obligation and shall be mitigated by investing in only the highest quality credits and by diversifying the investment portfolio so that the failure of any one issuer would not unduly harm the Authority’s cash flows.

(ii) Market risk is the risk of market value fluctuations due to overall changes in the general level of interest rates and shall be mitigated by:

(A) structuring the portfolio so that securities mature at the same time major cash outflows occur, thereby eliminating the need to sell securities prior to their maturity; and

(B) limiting the average maturity of the Authority's portfolio to three years and the maximum maturity of any one security in the portfolio to five years.

It is explicitly recognized, however, that in a diversified portfolio occasional losses may be inevitable and must be considered within the context of overall investment return.

(b) Liquidity. The Authority's investment portfolio will be structured to provide sufficient liquidity to meet the operating requirements of the Authority.

(c) Return on Investment. State law requires that the objective of return on investment be subordinate to the objectives of safety and liquidity. Therefore, investment officials shall seek to achieve a return on the funds under their control throughout all economic cycles, taking into consideration the Authority's investment risk constraints and cash flow requirements.

(3) Authority to Invest Funds.

(a) Policy principles for investment of Authority funds. Monies entrusted to the Authority will be invested and actively managed pursuant to applicable California statutory limitations and the guidance and limitations set forth in the Authority's written policies. Authority for the management and investment of Authority funds rests with the Authority Board of Directors ("Board"). The Board promulgates the policy for investment and management of Authority funds and conducts periodic reviews to ensure compliance with policy and statutory requirements. All persons authorized to make investment decisions for the Authority are trustees of the Authority and owe the Authority a fiduciary duty. All trustees are bound by the prudent investor rule, which requires trustees in making decisions with regards to the Authority's funds to 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. Trustees of Authority funds are relieved of personal responsibility for an individual security's risk or market price changes where the trustees at all times were acting in accordance with written procedures and this investment policy, exercising due diligence, taking timely and appropriate action to control adverse developments, and provided timely appropriate reports to the Board regarding the adverse developments with an investment.

(b) Delegation of investment authority to Treasurer. The Board delegates the authority to invest and manage the funds of the Authority to the Authority's Treasurer. Such delegation shall be on a fiscal year basis and subject to renewal by the Board, at its option, after appropriate review of the investment record. The Board reserves the right to revoke the delegation of investment authority at its discretion. On a monthly basis, the Treasurer shall report to the Board all investment transactions, whether purchases or sales, occurring since the last report. On a quarterly basis, the Treasurer shall report to the board the status of Authority's investment portfolio in accordance with section (10)(a) of this policy. Whenever a security is sold at a loss, the Treasurer will record the loss as such in the Authority's accounting system. The Treasurer shall designate in writing an officer or employee of the Authority who shall have authority to execute or authorize execution of an investment trade on behalf of the Authority when the Treasurer is not reasonably available and circumstances require timely action.

(c) Treasurer's responsibility for investments. Investment and management of the Authority's funds shall be solely the responsibility of the Authority's Treasurer, who shall take necessary measures to be fully informed on current market conditions and market trends in general and the condition of the Authority's investment portfolio in particular. The Treasurer shall establish and periodically review for currency and adequacy a system of controls to ensure compliance with the applicable statutory requirements and the Authority's investment policies. The system of controls shall also provide for regulation of subordinate officers and employees as well as investment advisors under contract with the Authority.

(d) Execution of trades by authorized investment advisor. Where the Board has approved a contract for a registered independent investment advisor to assist the Treasurer in the discharge of investment responsibilities and where the chief financial advisor has approved in writing a strategy to guide the investment of Authority funds, the Treasurer may authorize the investment advisor to execute trades on behalf of the Authority to effectuate the approved investment strategy. The Treasurer shall make such delegation via a document that specifies the boundaries of the delegated authorization. An investment advisor designated to execute trades on behalf of the Authority shall be bound by applicable policies of the Authority, and the investment advisor shall not execute any trade through any security broker in whom the investment advisor holds an ownership interest or has a financial interest. Authorizing the investment advisor to execute trades on behalf of the Authority does not relieve the Treasurer of responsibility for management and oversight of all investment transactions involving Authority funds. The Treasurer or designated Authority officer or employee, as provided in Section 3(b), when the Treasurer is not reasonably available and circumstances require timely action must approve in writing an investment transactions that exceed a market value of five million dollars (\$5,000,000) prior to execution of the trade. The investment advisor shall provide a written report of all trades made on behalf of the Authority to the Treasurer within twenty-four (24) hours of trade execution.

(4) Ethics and Conflicts of Interest. The Board, Authority officers or Authority employees involved in the investment process shall refrain from any activity that could conflict with proper execution of the investment program or which could impair the Authority's Treasurer's ability to make impartial investment decisions. Authority staff involved with the investment process shall disclose to the Authority Treasurer's any financial interest in financial institutions that conduct business with the Authority and they shall further disclose any personal financial and/or investment positions that could be related to the performance of the Authority's portfolio. Board members, Authority officials and Authority employees shall subordinate their personal investment transactions to those of the Authority, particularly with regard to the time of purchases and sales.

(5) Placement of Trade Execution Orders.

- (a) Whenever possible, investment transactions shall be made via a competitive process to ensure the Authority's security transactions are made on terms most favorable to the Authority. Trade execution shall be only through firms registered with the Financial Industry Regulatory Authority (FINRA) and approved by the Treasurer. To ensure security transactions are made via the most competitive process, solicitation of bids to transact a security trade shall be provided equally to all security dealers approved by the Treasurer pursuant to the section (5)(b) of this policy. This policy permits the Authority to purchase investments directly from approved issuers who require no competitive process (e.g., Local Agency Investment Fund (LAIF), the San Diego County Investment Pool (SDCIP), and Local Government Investment Pools (LGIPs).
- (b) The Treasurer shall maintain a list of security dealers approved to execute security trades on behalf of the Authority. Prior to approving a security dealer to execute security trades, the Treasurer shall determine that the dealer is fully qualified to execute security trades for the Authority. In evaluating whether a specific dealer is so qualified, the Treasurer shall evaluate, at a minimum, the dealer's security registration, financial condition, standing in the investment community, and experience with security trades of the nature to be executed on behalf of the Authority. To be qualified, all financial institutions and broker/dealers who desire to become qualified bidders for investment transactions must supply the following information on an annual basis: (1) audited financial statements; (2) proof of Financial Industry Regulatory Authority (FINRA) certification; (3) a trading resolution; (4) proof of California registration; and (5) a completed broker/dealer questionnaire.
- (c) Where the Board has approved a contract for a registered independent investment advisor to assist the Treasurer in the discharge of the investment responsibilities, the Treasurer may rely on the advisor's assurances that specific security dealers are fully qualified to execute trades on behalf of the Authority. The investment advisor shall provide such assurances in writing and shall renew the assurances based on an annual review of the financial condition and registrations of qualified bidders.

(6) Authorized Investments.

The Authority is authorized by the applicable sections of Cal. Gov. Code §53600 *et seq.* and §53630 *et seq.* to invest in the following types of securities, further limited herein:

(a) United States Treasury Bills, Bonds and Notes or those for which the full faith and credit of the United States are pledged for payment of principal and interest. There is no limitation as to the percentage of the portfolio that can be invested in this category. Cal. Gov. Code §53601(b) and 53635.2

(b) Federal agency or United States government-sponsored enterprise obligations, participations, or other instruments, including those issued by or fully guaranteed as to principal and interest by federal agencies or United States government-sponsored enterprises. There is no limitation as to the percentage of the portfolio that can be invested in this category. Cal. Gov. Code §53601(f) and 53635.2

(c) Bills of exchange or time drafts drawn on and accepted by a commercial bank, otherwise known as bankers acceptances which are eligible for purchase by the Federal Reserve System and are rated in the highest category by a nationally recognized statistical rating organization (NRSRO), may not exceed 180 days to maturity or 40% of the market value of the portfolio. No more than 10% of the market value of the portfolio may be invested in banker's acceptances issued by any one bank. Cal. Gov. Code §53601(g) and 53635.2

(d) Commercial paper of "prime" quality of the highest ranking or of the highest letter and number rating as provided for by a NRSRO. The entity that issues the commercial paper shall meet all of the following conditions in either paragraph (1) or paragraph (2):

(1) The entity meets the following criteria: (i) Is organized and operating in the United States as a general corporation. (ii) Has total assets in excess of five hundred million dollars (\$500,000,000). (iii) Has debt other than commercial paper, if any, that is rated "A" or higher by a NRSRO.

(2) The entity meets the following criteria: (i) Is organized within the United States as a special purpose corporation, trust, or limited liability company. (ii) Has program wide credit enhancements including, but not limited to, over collateralization, letters of credit, or surety bond. (iii) Has commercial paper that is rated "A-1" or higher, or the equivalent, by a NRSRO.

Eligible commercial paper shall have a maximum maturity of 270 days or less. No more than 25% of the market value of the portfolio ~~Authority's fund~~ may be invested in commercial paper. No more than 10% of the market value of the portfolio ~~Authority's funds~~ may be invested in the commercial paper of any single issuer. The amount invested in commercial paper of any one issuer in combination with any other securities from that issuer shall not exceed 10% of the market value of the portfolio. Cal. Gov. Code §53601(h) and 53635.2

(e) Negotiable Certificates of Deposit (NCDs) issued by a nationally or state-chartered bank or a state or federal savings institution. Purchased NCDs may not exceed 30% in aggregate of the market value of the portfolio. Negotiable Certificates of Deposit (NCDs) together with Placement Service Certificates of Deposit (PSCDs) may not exceed 30% in aggregate of the market value of the portfolio. NCDs eligible for purchase shall be rated "A" or better by a NRSRO. NCDs with an "A" rating shall be limited to 24 months maximum maturity; "AA" rated NCDs shall be limited to 36 months. The amount invested in NCDs of any one issuer in combination with any other securities from that issuer shall not exceed 10% of the market value of the portfolio. Cal. Gov. Code §53601(i) and 53635.2

(f) Placement Service Certificates of Deposit (PSCDs). Certificates of deposit placed through a deposit placement service that meet the requirements of Cal. Gov. Code §53601.8. The full amount of the principal and the interest that may be accrued during the maximum term of each certificate of deposit shall at all times be insured by federal deposit insurance. The maximum term for PSCDs shall be three years. An aggregate of 30% of the Authority's portfolio may be invested in PSCDs. Placement Service Certificates of Deposits (PSCDs) together with Negotiable Certificates of Deposit (NCDs) may not exceed 30% in aggregate of the market value of the portfolio. The amount invested in PSCDs of any one issuer in combination with any other securities from that issuer shall not exceed 10% of the market value of the portfolio. Cal. Gov. Code §53601.8 and 53635.8

(g) Bank Deposits, including, but not limited to, demand deposit accounts, savings accounts, market rate accounts and time certificates of deposits ("TCDs") in financial institutions located in California. The Authority will invest in financial institutions with a net worth of ten million dollars and total assets in excess of \$50 million. Such deposits in each bank shall be limited to no more than 5% of the total assets of the bank. To be eligible to receive Authority deposits, the financial institution must have received a minimum overall satisfactory rating, under the Community Reinvestment Act, for meeting the credit needs of California Communities in its most recent evaluation. Bank deposits are required to be collateralized as specified under Cal Gov. Code §53630 *et seq.* The Treasurer may waive the collateralization requirements for any portion that is covered by federal deposit insurance. The Authority shall have a signed agreement with any depository accepting Authority funds per Cal. Gov. Code §53649. The maximum maturity of TCDs is 1 year. A maximum of 20% of the market value of the Authority's portfolio may be invested in TCDs. The amount invested in TCDs of any one issuer in combination with any other securities from that issuer shall not exceed 10% of the market value of the portfolio. Cal. Gov. Code ~~§53601.8, 53649, 53653 and, 53635.2, and 53635.8~~

(h) Medium Term Notes (MTNs) and Long Term Notes (LTNs) with less than 5 years remaining until maturity shall be eligible for purchase shall be if rated "A" or better by a NRSRO and be issued by a corporation organized and operating within the United States. MTNs and LTNs with an "A" rating shall be limited to 24 months maximum maturity; "AA" rated MTNs and LTNs shall be limited to 36 months. The aggregate total of all purchased MTNs and LTNs may not exceed 15% of the market value of the investment portfolio. The amount invested in MTNs and LTNs of any one issuer in combination with any other securities from that issuer shall not exceed 10% of the market value of the portfolio. Cal. Gov. Code §53601(k) and 53635.2

(i) Repurchase agreements (RPAs) shall only be made with financial institutions having a credit rating of not less than "A". The Security Industry and Financial Markets Association (SIFMA) master repurchase agreement shall be the Authority's master repurchase agreement.

The term of the agreement may not exceed one year.

The following collateral restrictions will be observed: Only U.S. Treasury securities or Federal Agency securities, as described in 6(a) and 6(b) above, will be acceptable collateral. All securities underlying Repurchase Agreements must be delivered to the Authority's custodian bank versus payment or be handled under a tri-party repurchase agreement. The total of all collateral for each Repurchase Agreement must equal or exceed, on the basis of market value plus accrued interest, 102% of the total dollar value of the money invested by the Authority for the term of the investment. Since the market value of the underlying securities is subject to daily market fluctuations, the investments in repurchase agreements shall be in compliance if the value of the underlying securities is brought back up to 102% no later than the next business day. For any Repurchase Agreement with a term of more than one day, the value of the underlying securities must be reviewed on a regular basis.

Market value must be calculated each time there is a substitution of collateral.

The Authority or its trustee shall have a perfected first security interest under the Uniform Commercial Code in all securities subject to Repurchase Agreement. Cal. Gov. Code §53601(j) and 53635.2

(j) The Local Agency Investment Fund ("LAIF"), established by the State Treasurer for the benefit of local agencies and identified under Cal. Gov. Code §16429.1 *et seq.*, is authorized up to the maximum amount permitted by state law. The market value of the Authority's investment in LAIF may not exceed the LAIF statutory limit, if applicable. ~~may invest in LAIF up to the statutory limit, if applicable.~~

(k) The San Diego County Investment Pool (SDCIP) as authorized by Cal. Gov. Code §53684. The market value of the Authority's investment in SDCIP may not exceed the LAIF statutory limit, if applicable. ~~may invest in SDCIP up to the LAIF statutory limit.~~

(l) Shares of beneficial interest issued by a joint powers authority (Local Government Investment Pools or ("LGIPs")) organized pursuant to Cal. Gov. Code §6509.7 that meet the requirements of Cal. Gov. Code §53601(p). The market value of the Authority's investment in any LGIP may not exceed the LAIF statutory limit. ~~Investment is allowed up to the LAIF statutory limit.~~ Prior to investing, the Treasurer will complete a thorough investigation of the potential investment. Whenever the Authority has any funds so invested, the Treasurer shall maintain on-going monitoring including the following:

(i) Establish the investment is a legal investment under Cal. Gov. Code.

(ii) A description of eligible investment securities, and a written statement of investment policy and objectives. All investments must comply with the eligible investments outlined in this policy. In the event that any investments do not comply with the eligible investments outlined in this Policy, the Treasurer will assess the potential risk of a substantial investment loss related to the investment(s) not in compliance. If the

potential risk of investment loss exceeds \$10,000, as determined by the Treasurer and Authority's Investment Advisor, the Treasurer will, as soon as reasonably practicable, execute a plan to transfer funds out of the LGIP and into an authorized investment.

(iii) The issuer must have a current AAA_m rating, provide a constant dollar pool with a stated objective of maintaining a \$1 net asset value, meet an asset size of \$1 billion at the time of investment, and provide for third-party custody of portfolio assets.

(iv) A description of interest calculations and how it is distributed, and how gains and losses are treated.

(v) A description of how the securities are safeguarded (including the settlement processes), and how often the securities are priced and the program audited.

(vi) A description of who may invest in the program, the type and number of governmental participants, investor concentrations, what size deposit and withdrawal are allowed, and what time restrictions are placed on these deposits and withdrawals.

(vii) A schedule for receiving statements and portfolio listings.

(viii) Determination of how reserves, retained earnings, etc. are utilized by the fund.

(ix) A fee schedule, and when and how is it assessed. Cal. Gov. Code §53601(p).

(m) The Authority may place funds in shares of beneficial interest issued by diversified management companies that are money market funds registered with the Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. §80a-1 et seq.), investing in the securities and obligations. Investment in money market funds may not exceed 20% of the Authority's market value of the portfolio with no more than 10% of the market value of the portfolio in any single fund. Additionally, each selected fund shall be large enough that the Authority's investment does not constitute more than 5% of the total fund balance. To be eligible for investment, these companies shall either:

(i) Attain the highest ranking or the highest letter and numerical rating provided by not less than two of the three largest nationally recognized rating services, or

(ii) Retain an investment adviser registered with the Securities and Exchange Commission with not less than 5 years' experience investing in the securities and obligation market as authorized by Cal. Gov. Code §53601, subdivision (a) to (m), inclusive and with assets under management in excess of \$500,000,000. Cal. Gov. Code §53601(l)

(n) The Authority may invest in: (i) Registered state warrants or treasury notes or bonds of this state 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 this state; (ii) Registered treasury notes or bonds issued by 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 state; and (iii) Bonds, notes, warrants or other evidence of debt issued by a local agency or municipality located 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. Securities eligible for investment under this paragraph shall be rated at least "A" a NRSRO. Purchase of securities authorized by this subdivision may not exceed 20% of the Authority's portfolio. The amount invested with any one issuer shall not exceed 5% of the portfolio. Cal. Gov. Code §53601 (c), (d), (e).

(o) Any "AAA" rated United States Government Sponsored Enterprise issued mortgage-backed security with a maximum of five years' maturity. Purchase of securities authorized by this subdivision may not exceed 20% of the Authority's portfolio. Cal. Gov. Code §53601 (o).

(p) Permitted Investment for Bond Proceeds. All investment types listed above are authorized investments for bond proceeds with the addition of the following:

Investment agreement or guaranteed investment contract (a) with or guaranteed by a national or state chartered bank or savings and loan, an insurance company or other financial institution whose unsecured debt is rated in the highest short-term rating category (if the term of the Investment Agreement is less than three years) or in either of the two highest long-term Rating Categories (if the term of the Investment Agreement is three years or longer) by one or more of the Rating Agencies, or (b) which investment agreement or guaranteed investment contract is fully secured by obligations described in items (a) or (b) of this section which are the following:

- (i) Valued not less frequently than monthly and have a fair market value, exclusive of accrued interest, at all times at least equal to 103% of the principal amount of the investment, together with the interest accrued and unpaid thereon, and
- (ii) Held by any Federal Reserve Bank or a depository acceptable to the Treasurer or any Authority bond trustee, and
- (iii) Subject to a perfected first lien on behalf of the Authority or any bond trustee and free and clear from all third-party liens

(7) Prohibited Investments. Investments not described herein, including but not limited to, inverse floating rate notes, range notes, interest-only strips that are derived from a pool of mortgages, ~~and~~, common stocks and long term corporate notes or bonds are prohibited from use in this portfolio. The Authority shall not invest any funds in any security that could result in zero interest accrual and zero discount accretion if held to maturity. Investments that exceed five years to maturity require authorization by the Board at least 30 days prior to purchase. Cal. Gov. Code §53601.6.

(8) Safekeeping of Securities. To protect against potential losses by the collapse of individual securities dealers, all securities owned by the Authority shall be held in safekeeping by a third person bank trust department acting as agent for the Authority under the terms of a custody agreement executed by the bank and the Authority. All securities will be received and delivered using standard delivery versus payment procedures. The only exception to the foregoing shall be: (i) LAIF; (ii) the SDCIP; (iii) LGIPs; (iv) money market mutual funds, and

(v) Certificates of Deposits (TCDs, NCDs, & PSCDs), since the purchased securities are not deliverable. A record of these investments shall be held by the Treasurer.

All investment officers shall be bonded and all investment accounts subject to surprise audits performed no less than on a quarterly basis.

(9) Portfolio Limitations. Percentage limits and credit criteria are applied at the time of purchase. If a percentage-of-portfolio limitation is exceeded due to reduction in portfolio size, the affected securities may be held to maturity to avoid losses. When no loss is indicated, the Authority's Treasurer shall consider restructuring the portfolio basing the decision in part on the expected length of time the portfolio will be imbalanced. The Treasurer shall report all such imbalances in the monthly report to the Board.

(10) Reporting Requirements.

(a) In accordance with Cal. Gov. Code §53646, on a quarterly basis, the Authority's Treasurer shall prepare in accordance with GAAP and GASB 31 a report detailing investments and investment activity and transmit same to the Executive Officer, the Internal Auditor and the Board.

(i) The report shall be submitted within 30 days of the end of the quarter covered by the report.

(ii) The report shall include the type of investment, issuer, date of maturity, par and dollar amount invested on all securities, investments and monies held by the Authority.

(iii) The report shall include a description of any funds, investments, or programs that are under the management of contracted persons.

(iv) The report shall also include a current market value on a market-to-market basis as of the report date using an established identified independent source for the valuation.

(v) The report shall state compliance of the portfolio to the statement of investment policy or the manner in which it is not in compliance.

(vi) The report shall state the Authority's ability to meet its budgeted expenditure requirements for the next six months or to explain why sufficient money may not be available.

(b) In accordance with Cal. Gov. Code §53607, the Authority's Treasurer shall make a monthly report of investment transactions to the Board.

(11) Internal Control. The development of internal controls is a function of management. The Authority's Treasurer shall establish and document a system of internal controls that will provide reasonable assurance regarding the achievement of objectives in the following categories:

- Safeguarding assets
- Ensuring validity of financial records and reports
- Promoting adherence to policies, procedures, regulations and laws

- Promoting effectiveness and efficiency of operations

In addition, the Authority's Treasurer shall:

- (a) Establish an annual process of an independent review by an external examiner.

(b) ~~Shall develop~~ Develop performance standards. Those performance standards will be reviewed by the ~~Executive Officer~~ Treasurer and presented as an information item to the President/CEO & the Board. On a quarterly basis, as part of the reporting requirements the Authority's Treasurer shall report actual compared to the performance standard and any substantial deviations shall be explained.

(c) Review the Authority's investment policy annually at a public meeting and obtain Board approval and adoption of the policy to ensure its consistency with the Authority's objectives of preservation of principal, liquidity, rate of return and the policy's relevance to current law and financial and economic trends. The Authority's Treasurer is responsible for maintaining guidance over the Authority's investment policy and ensuring that the Authority can adapt readily to changing market conditions and shall submit to the Board any modification to the investment policy prior to implementation.

(12) Glossary of Terms.

Asked: The price at which securities are offered (that is, the price at which a firm will sell a security to an investor).

Bankers' Acceptance (BA): A draft or bill of exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the issuer.

Bid: The price offered for securities (that is, the price at which a firm will pay to purchase a security an investor owns).

Broker: A broker brings buyers and sellers together for a commission paid by the initiator of the transaction or by both sides; he does not take a position. In the money market, brokers are active in markets in which banks buy and sell money and in interdealer markets.

Certificate of Deposit (CD): See: Time Certificate of Deposits, Placement Service Certificate of Deposits, Negotiable Certificates of Deposits

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

Commercial Paper (CP) - An unsecured short-term promissory note issued by corporations and local governments, with maturities ranging from one to 270 days. Commercial paper is usually issued at a discount from par with a zero coupon. Highly-

rated, or "Prime" commercial paper carries an Standard & Poor's rating of A1 or A1+, a Moody's rating of P1, and/or a Fitch rating of F1 or F1+.

Constant Maturity Treasury (CMT) – A calculated average released by the Federal Reserve of all Treasury yields along a specific maturity point. This calculation is frequently used as a benchmark for conservative government portfolios.

Coupon: (a) The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value; (b) A certificate attached to a bond evidencing interest due on a payment date.

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

Debenture: A bond secured only by the general credit of the issuer.

Delivery versus Payment: There are two methods of delivery of securities: delivery versus payment and delivery versus receipt (also called free delivery). Delivery versus payment is delivery of securities with an exchange of money for the securities. Delivery versus receipt is delivery of securities with an exchange of a signed receipt for the securities.

Discount: The difference between the cost price of a security and its value at maturity when quoted at lower than face value. A security selling below original offering price shortly after sale also is considered to be selling at a discount.

Diversification: Dividing investment funds among a variety of securities offering independent returns.

Federal Farm Credit Bank (FFCB): The Federal Farm Credit Bank System is the oldest of the government sponsored enterprises, created by an act of Congress in 1916. Its mission is to provide a reliable and low cost source of funds to support agriculture in the United States. FFCB debt obligations are highly liquid and its senior debt is AAA-rated.

Federal Home Loan Banks: ~~The institutions that regulate and lend to savings and loan associations. The Federal Home Loan Banks play a role analogous to that played by the Federal Reserve Banks vis à vis member commercial banks.~~ The Federal Home Loan Bank was created by an act of Congress in 1932 as a system of 12 regional banks that provide funds to its member banks. FHLB's primary mission is to support residential and community lending. Its membership of more than 8,000 financial institutions includes savings banks, commercial banks, credit unions and insurance companies active in housing finance. FHLB debt obligations are highly liquid and its senior debt is AAA-rated.

Federal Home Loan Mortgage Company (FHLMC or “Freddie Mac”): Freddie Mac was created by an act of Congress in 1970 as a shareholder-owned company to further expand the secondary market for mortgage loans in the United States. Freddie Mac buys existing mortgages and pools them together to create mortgage-backed securities that can then be sold to investors, thereby providing liquidity to lenders who can then make additional loans. Along with Fannie Mae, Freddie Mac was placed into government conservatorship in September 2008, but continues full operations under government control and has been instrumental in the government’s attempts to revive the housing sector. Freddie Mac securities are highly liquid and its senior debt is AAA-rated.

Federal National Mortgage Association (FNMA): Fannie Mae was created by an act of Congress in 1938 under the Federal National Mortgage Association Act to provide a secondary market for mortgage loans in the United States. It does this by purchasing existing home loans and pooling them together to create mortgage-backed securities that can then be sold to investors, along with a guaranty of the timely payment of principal and interest on the underlying loans. Fannie Mae was privatized in 1968, and operated as a private stockholder-owned company for 40 years before the housing market collapse forced them into federal government conservatorship in September 2008. Fannie Mae debt obligations are highly liquid and its senior debt is AAA-rated.

Government National Mortgage Association (GNMA or Ginnie Mae): Securities guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loan associations and other institutions. Security holder is protected by full faith and credit of the U.S. Government. Ginnie Mae securities are backed by FHA or VA mortgages. The term pass-through is often used to describe Ginnie Maes.

Inverse Floating Rate Note: A debt security with an interest rate stated as a fixed rate minus an index. This calculation causes the rate on the inverse floater to move in the opposite direction of general interest rates. This instrument generally performs well in a declining interest rate environment but will lose value if rates rise.

Liquidity: A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value. In the money market, a security is said to be liquid if the spread between the bid and asked prices is narrow and reasonable size can be done at those quotes.

Local Government Investment Pools (LGIPs): Shares of beneficial interest issued by a joint powers authority organized pursuant to Cal. Gov. Code §6509.7. LGIPs offer a diversification alternative to LAIF and SDCIP for short term cash management facilities.

Market Value: The price at which a security is trading and could presumably be sold.

Master Repurchase Agreement: A written contract covering all future transactions between the persons to repurchase agreements and reverse repurchase agreements that establish each person’s rights in the transactions. A master agreement will often specify,

among other things, the right of the buyer-lender to liquidate the underlying securities in the event of default by the seller-borrower.

Maturity: The date upon which the principal or stated value of an investment becomes due and payable.

Medium Term Notes: A class of debenture that is defined as all corporate and depository debt securities with a maximum remaining maturity of five years or less.

Money Market: The market in which short-term debt instruments (bills, commercial paper, bankers' acceptance, etc.) are issued and traded.

Negotiable Certificate of Deposit (NCD): A type of CD that is at least \$100,000 and can also be traded on a highly liquid secondary market.

Placement Service Certificates of Deposit (PSCD): A type of CD that uses a deposit placement service. The placement service will allow the bank with which the investment is placed to split the initial deposit into multiple pieces that are then distributed among a network of banks, such that the full amount of the deposit is protected by the FDIC insurance of each participating bank.

Portfolio: Collection of securities held by an investor.

Primary Dealer: A group of government securities dealers that submit daily reports of market activity and positions and monthly financial statements to the Federal Reserve Bank of New York and are subject to its informal oversight. Primary dealers include Securities and Exchange Commission (SEC) registered securities, broker/dealers, banks and a few unregulated firms.

Prudent Investor Standard: An investment standard. In some states the law requires that a fiduciary, such as a trustee, may invest money only in a list of securities selected by the state, the so-called legal list. In other states, the trustee may invest in a security if it is one that would be bought by a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital.

Range Note: A debt security with a varied interest payment that depends on the number of days the designated index falls within (or in some cases outside) an established range of interest rates. Should rates move beyond the range on either end, the investor faces the risk of a reduced or zero interest payment for the applicable interest period.

Rate of Return: The yield obtainable on a security based on its purchase price or its current market price.

Rating Agency: Nationally recognized credit rating agency such as Fitch, Moody's or S&P.

Rating Category: A credit rating assignment by a Rating Agency shall mean (a) with respect to any long-term rating category, all ratings designated by a particular letter or combination of letters, without regard to any numerical modifier, plus or minus sign or other modifier, and (b) with respect to any short-term or commercial paper rating category, all ratings designated by a particular letter or combination of letters and taking into account any numerical modifier, but not any plus or minus sign or other modifier.

Repurchase Agreement (RP or Repo): A holder of securities sells these securities to an investor with an agreement to repurchase them at a fixed price on a fixed date. The security "buyer" in effect lends the "seller" money for the period of the agreement and the terms of the agreement are structured to compensate the buyer for this. Dealers use RP extensively to finance their positions. Exception: when the Fed is said to be doing RP, it is lending money, which is increasing bank reserves.

Safekeeping: A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank's vaults for protection.

Sec Rule 15C3-1: See Uniform Net Capital Rule.

Securities and Exchange Commission: Agency created by Congress to protect investors in securities transactions by administering securities legislation.

Strip (Bonds): Brokerage-house practice of separating a bond into its principal and interest, which are then sold as zero coupon bonds.

Time Certificate of Deposit (CD): A time deposit with a specific maturity evidenced by a certificate. Large denomination CDs are typically negotiable.

Treasurer: The Vice President of Finance /Treasurer of the Authority or the authorized designee or representative as designated by the President/Chief Executive Officer.

Treasury Bill: A non-interest bearing discount security issued by the U.S. Treasury to finance the national debt. Most bills are issued to mature in three months, six months or one year.

Treasury Bond: Long-term U.S. Treasury security having initial maturities of more than ten years.

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

Yield: The rate of annual income return on an investment, expressed as a percentage. (A) **Income Yield** is obtained by dividing the current dollar income by the current market price for the security. (B) **Net Yield or Yield to Maturity** is the current income yield minus any premium above par or plus any discount from par in purchase price, with the

adjustment spread over the period from the date of purchase to the date of maturity of the bond.

- | [Amended by Resolution No. 2011- dated June 2, 2011]
- [Amended by Resolution No. 2010-0059 dated June 3, 2010]
- [Amended by Resolution No. 2009-0123 dated October 1, 2009]
- [Amended by Resolution No. 2008-0118 dated September 4, 2008]
- [Amended by Resolution No. 2006-0010 dated February 6, 2006]
- [Amended by Resolution No. 2005-0102 dated September 8, 2005]
- [Amended by Resolution No. 2004-0133 dated December 6, 2004]
- [Amended by Resolution No. 2004-0100 dated October 4, 2004]
- [Amended by Resolution No. 2004-0032 dated April 5, 2004]
- [Resolution No. 2002-02 dated September 20, 2002]

San Diego County Regional Airport Authority

Review of the Investment Policy

&

Delegation of Authority to Vice President,
Finance/Treasurer for Investing Funds

Presented by:

Vernon D. Evans, CPA

Vice-President-Finance/Treasurer and CFO



Investment Policy

- Serves as the foundation of investment goals and objectives
- Mandates investing in a manner that provides the highest security while meeting Authority cash flow needs
- Demonstrates our fiduciary responsibility, thereby promoting trust and confidence from the public we serve
- Adheres to and exceeds the requirements of California Government Code Section 53600 et seq

Investment Policy

- Adheres to state law requirements that return on investment be subordinate to objectives of safety and liquidity
- Developed and annually reviewed in conjunction with our financial and investment advisors
- Annual Board review is not required by State Code, but is an Authority practice
- Awarded Investment Policy Certificate of Excellence Award in 2008 and 2010 by Association of Public Treasurers of United States and Canada. Investment Policy will be submitted for the 2011 award in June.

Investment Policy - Amendments

- *Changed language from 'Authority funds' to 'Market value of the portfolio' in the following sections:*
 - 'Market value of the portfolio' is more specific about which calculated value is used when measuring each investment against the Portfolio's guidelines.
 - (6)(d) *Commercial Paper*
 - (6)(g) *Bank Deposits*
 - (6)(j) *Local Agency Investment Fund*
 - (6)(k) *San Diego County Investment Pool*
 - (6)(l) *Local Government Investment Pools*
 - (6)(m) *Money Market Funds*

Investment Policy - Amendments

- *Section (6)(e) Negotiable Certificates of Deposit:*

Revised portfolio limit from 30% in Negotiable CDs to 30% in Negotiable CDs and Placement Service CDs.

– “ ~~Purchased NCDs may not exceed 30% in aggregate of the market value of the portfolio.~~ Negotiable Certificates of Deposit (NCDs) together with Placement Service Certificates of Deposit (PSCDs) may not exceed 30% in aggregate of the market value of the portfolio. ”

- *Section (6)(f) Placement Service Certificates of Deposit:*

Revised portfolio limit from 30% in Placement Service CDs to 30% in Placement Service CDs and Negotiable CDs.

– “ ~~An aggregate of 30% of the Authority's portfolio may be invested in PSCDs.~~ Placement Service Certificates of Deposit (PSCDs) together with Negotiable Certificates of Deposit (NCDs) may not exceed 30% in aggregate of the market value of the portfolio. ”

Investment Policy - Amendments

- *Section (6)(g) Bank Deposits:*

Removed reference to government code that were not directly related to Bank Deposits.

–“ A maximum of 20% of Authority’s portfolio may be invested in TCDs. The amount invested in TCDs of any one issuer in combination with any other securities from that issuer shall not exceed 10% of the market value of the portfolio. Cal. Gov. Code §~~53601.8,~~ 53649, 53653 **and** 53635.2. **and 53635.8.**”



Investment Policy - Amendments

- *Section (6)(h) Medium Term Notes (MTNs):*

Added language to allow for Long Term Notes (LTNs) with less than 5 years remaining until maturity.

–“Medium Term Notes (MTNs) **and Long Term Notes (LTNs) with less than 5 years remaining until maturity shall be** eligible for purchase **shall be if** rated “A” or better by a NRSRO and be issued by a corporation organized and operating within the United States. MTNs **and LTNs** with an “A” rating shall be limited to 24 months maximum maturity; “AA” rated MTNs **and LTNs** shall be limited to 36 months. The aggregate total of all purchased MTNs **and LTNs** may not exceed 15% of the market value of the investment portfolio. The amount invested in MTNs **and LTNs** of any one issuer in combination with any other securities from that issuer shall not exceed 10% of the market value of the portfolio. Cal. Gov. Code §53601(k) and 53635.2.”

Investment Policy - Amendments

- *Section (6)(l)(ii) Local Government Investment Pools:*

Added language to provide guidance and procedures in the event that a Local Government Investment Pool that the Authority has invested in falls out of compliance with the Authority's investment policy.

–“A description of eligible investment securities, and a written statement of investment policy and objectives. All investments must comply with the eligible investments outlined in this policy. **In the event that any investments do not comply with the eligible investments outlined in this Policy, the Treasurer will assess the potential risk of a substantial investment loss related to the investment(s) not in compliance. If the potential risk of investment loss exceeds \$10,000, as determined by the Treasurer and Authority's Investment Advisor, the Treasurer will, as soon as reasonably practicable, execute a plan to transfer funds out of the LGIP and into an authorized investment.”**

Investment Policy - Amendments

- *Section (6)(l)(iii) Local Government Investment Pools:*
 - Changed credit rating requirement from 'AAA' to 'AAAm' to reflect the new rating system for money market funds.
 - “The issuer must have a current **AAAm** rating, provide a constant dollar pool with a stated objective of maintaining a \$1 net asset value, meet an asset size of \$1 billion at the time of investment, and provide for third-party custody of portfolio assets.”



Investment Policy - Amendments

- *Section (7) Prohibited Investments:*

Removed restrictions on long-term corporate notes or bonds to allow for investment in long-term notes & bonds with remaining maturities of less than five years.

–“Prohibited Investments. Investments not described herein, including but not limited to, inverse floating rate notes, range notes, interest-only strips that are derived from a pool of mortgages, ~~and common stocks and long-term corporate notes or bonds~~ are prohibited from use in this portfolio. The Authority shall not invest any funds in any security that could result in zero interest accrual and zero discount accretion if held to maturity. Investments that exceed five years to maturity require authorization by the Board at least 30 days prior to purchase. Cal. Gov. Code §53601.6.”

Investment Policy - Amendments

- *Section (8) Safekeeping of Securities:*

Removed Negotiable Certificates of Deposit (NCDs) from the list of securities exempted from the safekeeping requirement. NCDs are deliverable securities and require safekeeping by a third party.

–“To protect against potential losses by the collapse of individual securities dealers, all securities owned by the Authority shall be held in safekeeping by a third person bank trust department acting as agent for the Authority under the terms of a custody agreement executed by the bank and the Authority. All securities will be received and delivered using standard delivery versus payment procedures. The only exception to the foregoing shall be: (i) LAIF; (ii) the SDCIP; (iii) LGIPs; (iv) money market mutual funds, and (v) Certificates of Deposits (TCDs, ~~NCDs~~, & PSCDs), since the purchased securities are not deliverable. A record of these investments shall be held by the Treasurer.”

Investment Policy - Amendments

- *Section (11)(b) Internal Control:*

Revised language to indicate the Treasurer's responsibility to review performance standards and present them to the President/CEO & Board.

–“~~Shall d~~Develop performance standards. Those performance standards will be reviewed by the ~~Executive Officer~~ Treasurer and presented as an information item to the ~~President/CEO and the~~ Board. On a quarterly basis, as part of the reporting requirements the Authority's Treasurer shall report actual compared to the performance standard and any substantial deviations shall be explained.”

Investment Policy - Amendments

- *Section (12) Glossary of Terms:*

Added definitions of the following terms:

- Commercial Paper (CP)
- Constant Maturity Treasury (CMT)
- Federal Farm Credit Bank (FFCB)
- Federal Home Loan Mortgage Company (FHLMC)

Modified definitions of the following terms:

- Federal Home Loan Banks
- Federal National Mortgage Association (FNMA)

Delegation of Investment Authority

- The Board delegates the authority to invest and manage funds to the Vice President of Finance / Treasurer
- This delegation is on a fiscal year basis and subject to renewal by the Board

Agenda Item Requests

- Agenda item is requesting that the Finance Committee forward the following recommendations to the Board for approval:
 - Approval of amendment to investment policy
 - Annual delegation of authority to invest and manage Authority funds to the Vice President of Finance / Treasurer

Questions

