

Medford Water Commission Investment Policy



Resolution #1710

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INVESTMENT POLICY FOR MEDFORD WATER COMMISSION

1. INTRODUCTION

This Investment Policy defines the parameters within which funds are to be invested by the Medford Water Commission. The Medford Water Commission is an autonomous agency of the City of Medford whose purpose is to furnish water for the City of Medford. This policy also formalizes the framework, pursuant to ORS 294.135, for the Medford Water Commission's investment activities to ensure effective and judicious management of funds within the scope of this policy.

These guidelines are intended to be broad enough to allow designated investment staff and investment advisor to function properly within the parameters of responsibility and authority, yet specific enough to adequately safeguard the investment assets.

2. GOVERNING AUTHORITY

The Medford Water Commission's investment program shall be operated in conformance with Oregon Revised Statutes and applicable Federal Law. Specifically, this investment policy is written in conformance with ORS 294.035; 294.040; 294.052, 294.135; 294.145; and 294.810. All funds within the scope of this policy are subject to regulations established by the state of Oregon. Any revisions or extensions of these sections of the ORS shall be assumed to be part of this Investment Policy immediately upon being enacted.

3. SCOPE

This policy applies to activities of the Medford Water Commission with regard to investing the financial assets of operating funds and capital funds. Investments of employees' retirement funds, deferred compensation plans and other funds are not covered by this policy. The amount of funds falling within the scope of this policy over the next three years is expected to range between \$15 million and \$25 million.

4. OBJECTIVES

The primary objectives, in priority order, of investment activities shall be:

4.1 Preservation of Capital:

Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The goal is to mitigate credit risk and interest rate risk.

4.2 Liquidity:

The investment portfolio shall remain sufficiently liquid to meet all reasonably anticipated operating requirements. Furthermore, the portfolio should consist largely of securities with active secondary or resale markets. A portion of the portfolio also may be placed in the Oregon Short Term Fund which offers next-day liquidity. Where possible and prudent, the portfolio should be structured so that investments mature concurrent with anticipated demands.

4.3 Return:

The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into consideration the safety and liquidity needs of the portfolio. Although return consists of both principal return (gains and losses due to market value fluctuations) and income return (yield), this policy discourages active trading and turnover of investments. Investments should generally be held to maturity.

5. STANDARDS OF CARE

5.1 Prudence:

The standard of prudence to be used by investment officials shall be the "prudent person" standard and shall be applied in the context of managing an overall portfolio. Investment officers acting in accordance with written procedures and this investment policy and exercising due diligence shall be relieved of personal liability for an individual security's credit risk or market price changes, provided deviations from expectations are reported and appropriate action is taken to control adverse developments within a timely fashion as defined in this policy. The "prudent person" standard states:

"Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived."

5.2 Ethics and Conflicts of Interest:

Officers and employees involved in the investment process shall refrain from personal activity that could conflict with the proper execution and management of the investment program, or that could impair their ability to make impartial decisions. Employees and investment officials shall disclose any material interests in financial institutions with which they conduct business. Disclosure shall be made to the Board of Water Commissioners. They shall further disclose any personal financial/investment positions that could be related to the performance of the investment portfolio. Employees and officers shall refrain from undertaking personal investment transactions with the same individual with whom business is conducted on behalf of the Medford Water Commission. Officers and employees shall, at all times, comply with the State of Oregon Government Standards and Practices code of ethics set forth in ORS Chapter 244.

5.3 Delegation of Authority and Responsibilities:

Governing Body:

The Board of Water Commissioners will retain ultimate fiduciary responsibility for invested funds. The Board will receive reports pursuant to and with sufficient detail to comply with ORS 294.085 and 294.155.

Delegation of Authority:

Authority to manage investments within the scope of this policy and operate the investment program in accordance with established written procedures and internal controls is granted to the Manager hereinafter referred to as Investment Officer, and derived from the following: ORS 294.035 to 294.053, 294.125 to 294.145, and 294.810.

No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the Investment Officer. The Investment Officer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

All participants in the investment process shall seek to act responsibly as custodians of the public trust. No officer or designee may engage in an investment transaction except as provided under the terms of this policy and supporting procedures.

Investment Committee:

The Board of Water Commissioners will function as the investment committee to provide guidance to the Investment Officer and monitor investment policy compliance.

Investment Advisor:

The Medford Water Commission may engage the services of an external investment manager to assist in the management of the investment portfolio in a manner consistent with this policy. The Investment Advisor may only be granted non-discretionary authority, requiring approval to purchase and sell securities. The advisor may be authorized to transact directly with approved dealer relationships on behalf of the Medford Water Commission.

6. TRANSACTION COUNTERPARTIES

6.1 Broker/Dealers:

The Investment Officer shall determine which broker/dealer firms and registered representatives are authorized for the purposes of investing funds within the scope of this investment policy. A list will be maintained of approved broker/dealer firms and affiliated registered representatives.

The following minimum criteria must be met prior to authorizing investment transactions with broker/dealer firms and affiliated registered representatives. The following minimum criteria must be met prior to authorizing investment transactions. The Investment Officer may impose more stringent criteria:

Broker/Dealer firms must meet the following minimum criteria:

- a) Be registered with the Securities and Exchange Commission (SEC)
- b) Be registered with the Financial Industry Regulatory Authority (FINRA)
- c) Provide most recent audited financials
- d) Provide FINRA Focus Report filings

Approved broker/dealer employees who execute transactions with the Medford Water Commission must meet the following minimum criteria:

- a) Be a registered representative with FINRA
- b) Be licensed by the State of Oregon
- c) Certify in writing having read, understood, and agreed to comply with the most current version of this investment policy
- d) Have notified the Medford Water Commission within 30 days of the initiation of any formal investigation or disciplinary action initiated by the federal or state regulators.

The Investment Officer will conduct at least annual reviews of all listed broker/dealers and their respective authorized registered representatives.

Factors considered would include but not be limited to:

- Pending investigations by securities regulators.
- Significant changes in net capital.
- Pending customer arbitration cases.
- Regulatory enforcement actions.

If the Medford Water Commission's investment advisor is contracted to provide securities transactions on behalf of the Medford Water Commission, the advisor's broker/dealer list must be provided to the Custodial Officer for approval. The Custodial Officer can assign the responsibility of broker/dealer due diligence process to the Advisor, and all licensing information on the counterparties will be maintained by the Advisor and available upon request.

The advisor broker/dealer review should include:

- i. FINRA Certification check
- ii. Firm Profile
- iii. Firm History
- iv. Firm Operations
- v. Disclosures of Arbitration Awards, Disciplinary and Regulatory Events
- vi. State Registration Verification
- vii. Financial review of acceptable FINRA capital requirements or letter of credit for clearing settlements.

The advisors must provide the Medford Water Commission with any changes to the list prior to transacting on behalf of the Medford Water Commission.

6.2 Investment Advisors:

An Investment Advisor may be selected by conducting a process of due diligence. The following items are required for the approved Investment Advisors:

- a) The Investment Advisor firm must be registered with the Securities and Exchange Commission (SEC) or licensed by the state of Oregon.
- b) All Investment Advisor firm representatives conducting investment transactions on behalf of the Medford Water Commission must be registered representatives with FINRA.
- c) All Investment Advisor firm representatives conducting investment transactions on behalf of the Medford Water Commission must be licensed by the state of Oregon.
- d) Contract terms will include that the Investment Advisor comply with the Commissions Investment Policy.
- e) All engaged Investment Advisors must provide notification within 30 days of any formal investigation or disciplinary action initiated by federal or state regulators.

The Investment Officer will conduct at least annual reviews of engaged Investment Advisors to determine their continued eligibility within the guidelines of this policy. The Investment Advisor must notify the Medford Water Commission immediately if any of the following issues arise while serving under a Medford Water Commission contract:

- a) Pending investigations by securities regulators

- b) Significant changes in net capital
- c) Pending customer arbitration cases
- d) Regulatory enforcement actions

The Medford Water Commission will seek investment advisory services through an RFP process.

6.3 Depositories:

All financial institutions who desire to become depositories must be qualified Oregon Depositories pursuant to ORS Chapter 295.

6.3 Competitive Transactions:

- a) The Investment Officer shall obtain and document competitive bid information on all investments purchased or sold in the secondary market. Competitive bids or offers should be obtained, when possible, from at least three separate brokers/financial institutions or through the use of a nationally recognized trading platform.
- b) In the instance of a security for which there is no readily available competitive bid or offering on the same specific issue, then the Investment Officer shall document quotations for comparable or alternative securities.
- c) When purchasing original issue instrumentality securities, no competitive offerings will be required as all dealers in the selling group offer those securities at the same original issue price. However, the Investment Officer shall document quotations on comparable securities.
- d) If an Investment Advisor provides investment management services, the Advisor must retain documentation of competitive pricing execution on each transaction and provide upon request.

7. ADMINISTRATION AND OPERATIONS

7.1 Delivery vs. Payment:

All trades of marketable securities will be executed (cleared and settled) by delivery versus payment to ensure that securities are deposited in the Medford Water Commission's safekeeping institution prior to the release of funds. The Medford Water Commission will have online access through the safekeeping bank for verification of the account holdings and transactions.

7.2 Third party Safekeeping:

Securities will be held by an independent third-party safekeeping institution selected by the Medford Water Commission. Upon request, the safekeeping institution shall make available a copy of its Statement on Standards for Attestation Engagements (SSAE) No. 16.

7.3 Internal Controls:

The Investment Officer and the Medford Water Commission are responsible for establishing and maintaining an adequate internal control structure designed to reasonably assure that invested funds are invested within the parameters of this Investment policy and protected from

loss, theft or misuse. Specifics for the internal controls shall be documented in writing. The established control structure shall be reviewed and updated periodically by the Investment Officer.

The internal controls shall address, at a minimum, the following:

- a) Compliance with Investment Policy
- b) Control Collusion
- c) Separation of transaction authority from accounting and record keeping
- d) Custodial safekeeping
- e) Avoidance of physical delivery of securities whenever possible and address control requirements for physical delivery when necessary
- f) Clear delegation of authority to subordinate staff members
- g) Confirmation of transaction for investment and wire transfers in written or digitally verifiable electronic form.
- h) Dual authorization of wire transfers and ACH's
- i) Staff training
- j) Review, maintenance, and monitoring of security procedures both manual and automated

7.4 Annual Independent Review:

An external auditor shall provide an annual independent review to assure compliance with Oregon state law and Medford Water Commission policies and procedures.

8. AUTHORIZED AND SUITABLE INVESTMENTS

8.1 Investment Types and Credit Guidelines:

All investments of the Medford Water Commission shall be made in accordance with Oregon Revised Statutes: ORS 294.035 (Investment of surplus funds of political subdivisions; approved investments), ORS 294.040 (Restriction on investments under ORS 294.035), ORS 294.135 (Investment maturity dates), ORS 294.145 (Prohibited conduct for Treasurer including not committing to invest funds or sell securities more than 14 business days prior to the anticipated date of settlement), ORS 294.805 to 294.895 (State Investment Pool). Bond proceeds may be invested under guidance of ORS 294.052. If additional types of securities are considered for investment, per Oregon state statute they will not be eligible for investment until this Policy has been amended and adopted by the Board of Water Commissioners.

The following investments are permitted pursuant to ORS 294.035, 294.040, and ORS 294.810.

This policy recognizes S&P and Moody's as the major Nationally Recognized Statistical Ratings Organizations (NRSRO).

In the case of split ratings, where the major NRSROs issue different ratings, the lower rating shall apply. Minimum credit ratings and percentage limitations apply to the time of purchase.

The Medford Water Commission is empowered to invest in the following types of securities:

US Treasury Obligations: U.S. Treasury and other government obligations that carry the full faith and credit guarantee of the United States for the timely payment of principal and interest. [ORS Section 294.035(3)(a)]

US Agency Obligations - Primary: Senior debenture obligations of US federal agencies and instrumentalities or U.S. government-sponsored enterprises (GSE) that have actively traded markets and provide a higher level of liquidity. These include Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC), Federal Home Loan Banks (FHLB), and the Federal Farm Credit Bureau (FFCB).

US Agency Obligations - Secondary: Other US government sponsored enterprises that are less marketable are considered secondary GSEs. They include but are not limited to: Private Export Funding Corporation (PEFCO), Tennessee Valley Authority (TVA), Financing Corporation (FICO) and Federal Agricultural Mortgage Corporation, (Farmer Mac). Securities must be rated by S&P or Moody's.

Municipal Debt: Lawfully issued debt obligations of the States of Oregon, California, Idaho and Washington and political subdivisions of those states if the obligations have a long-term rating on the settlement date of AA- or better by S&P or Aa3 or better by Moody's.

Corporate Indebtedness: Corporate indebtedness must be rated on the settlement date AA- or better by S&P or Aa3 or better by Moody's [ORS 294.035(3)(B)].

Commercial Paper: Commercial Paper that is rated A1+ by Standard and Poor's and P1 Moody's. Issuer constraints for commercial paper combined with corporate notes will be limited by statute to 5% of market value per issuer.

Certificates of Deposit: Certificates of deposit in insured institutions as defined in ORS Section 706.008, in credit unions as defined in ORS Section 723.006, or in federal credit unions, if the institution or credit union maintains a head office or a branch in this state [ORS Section 294.035(3)(d)].

Bank Time Deposits/Savings Accounts: Bank Time Deposits and savings accounts in insured institutions as defined in ORS Section 706.008, in credit unions as defined in ORS Section 723.006, or in federal credit unions, if the institution or credit union maintains a head office or a branch in this state [ORS Section 294.035(3)(d)].

Banker's Acceptance: A short-term credit investment created by a non-financial firm and guaranteed by a qualified financial institution whose long-term letter of credit rating must have an A1+ rating by S&P or P1 from Moody's.

Oregon Short Term Fund: The Oregon Short Term Fund (OSTF), also named the Local Government Investment Pool (LGIP), is an open-ended, no-load diversified portfolio offered to eligible participants that includes, but is not limited to, any municipality, political subdivision or public corporation of the State of Oregon that by law is made the custodian of, or has control of, any public funds. The LGIP is commingled with the State of Oregon's short-term funds. Oregon's LGIP was created by ORS Chapter 748. The OSTF is allowed to invest up to 50% of the funds in Corporate securities down to a single A rating. The maximum maturity is 3 years, and 50% of the pool must mature or reset within 93 days. The portfolio is managed

by Treasury professionals at the State of Oregon. The fund is expected to maintain \$1.00 per every dollar put into the fund, but \$1.00 Net Asset Value is not guaranteed. The Commission's total fund balance held in the pool is limited by statute.

8.2 Collateralization:

Repurchase Agreements:

- a) ORS 294.035 (3) requires repurchase agreement collateral to be limited in maturity to three years and priced according to percentages prescribed by written policy of the Oregon Investment Council or the Oregon Short Term Fund Board.
- b) ORS 294.135 (3) limits the maximum term of any repurchase agreement to 90 days.
- c) The following margins are required:
 - US Treasury Securities: 102%
 - US Agency Discount and Coupon Securities: 102%
 - Mortgage Backed and Other*: 103%

*Limited to those securities described in ORS 294.035(1)

8.3 Prohibited Investments:

- 8.3.1 US Agency Mortgage-backed Securities:
US agency mortgage-backed securities such as those securities by FNMA and FHLMC are not allowed.
- 8.3.2 Commercial Paper:
Asset Backed Commercial paper is not allowed.
- 8.3.3 Private Placement or "144A" Securities:
Private placement or "144A" securities are not allowed. This includes commercial paper issued under section 4(2)144A (also known as "4(2)A") of the Securities Act of 1933.
- 8.3.4 Securities Lending and Reverse Repurchase Agreements:
The Medford Water Commission shall not lend securities nor directly participate in a securities lending or reverse repurchase program.

9. INVESTMENT PARAMETERS

9.1 Credit Risk:

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

- a. Diversification: It is the policy of the Medford Water Commission to diversify its investments. Where appropriate, exposures will be limited by security type, maturity, issuance, issuer and security type. Allowed security types and investment exposure limitations are detailed in the table below.
- b. Investment Credit Ratings: Investments must have a rating from at least one of the following nationally recognized statistical ratings organizations: Moody's Investors Service, Standard & Poor's or Fitch Ratings Service as detailed in the table below.

Ratings used to apply the guidelines below should be investment level ratings and not issuer level ratings.

- c. Restriction on Municipal Issuers with Prior Default History:
Per ORS 294.040, the bonds of issuers listed in ORS 294.035 (3)(a) to (c) may be purchased only if there has been no default in payment of either the principal or the interest on the obligations of the issuing Commission, port, school district or city, for a period of twenty years next preceding the date of the investment.

Exposure Constraints:

Issue Type	Maximum % Holdings	Maximum % per Issuer	Ratings S&P	Ratings Moody's
US Treasury Obligations	100%	None	N/A	N/A
US Agency Primary Securities FHLB, FNMA, FHLMC, FFCB	100%	33%	N/A	N/A
US Agency Secondary Securities FICO, FARMER MAC etc.	10%	10%	Security must be rated	Security must be rated
Municipal Bonds (OR, CA, ID, WA)	10%	10%	AA-	Aa3
Corporate Bonds	15%	5%*	AA-	Aa3
Commercial Paper	15%		A1+	P1
Certificates of Deposit	20%	5%	Oregon Public Depository	Oregon Public Depository
Bank Time Deposits/Savings Accounts	50%	25%	Oregon Public Depository	Oregon Public Depository
Banker's Acceptance	25%	5%	A1+ AA- Underlying	P1 Aa3 Underlying
Oregon Short Term Fund	Maximum allowed per ORS 294.810	None	N/A	N/A

**Issuer constraints apply to the combined issues in corporate and commercial paper holdings.*

9.2 Liquidity Risk:

Liquidity risk is the risk that there that there may not be enough cash balances available to provide for demand payments. The following strategies will be employed to mitigate liquidity risks:

- a. The amount of at least 10% of funds available for investing will be invested in the Oregon Short Term Fund, with a qualified depository institution, or investments maturing in less than 30 days to provide sufficient liquidity for expected disbursements.
- b. Reserve or Capital Improvement Project monies may be invested in securities exceeding the maximum term if the maturities of such investments are made to coincide as nearly as practicable with the expected use of the funds.

- c. Operating funds in excess of liquidity requirements will be invested subject to the Total Portfolio Maturity Constraints following. Portfolio investment maturities will be limited as follows:

Total Portfolio Maturity Constraints:

Maturity Constraints	Minimum % of Total Portfolio
Under 30 days	10%
Under 1 year	25%
Under 5 years	100%
Maturity Constraints	Maximum of Total Portfolio in Years
Weighted Average Maturity	2.00
Security Structure Constraint	Maximum % of Total Portfolio
Callable Agency Securities	25%

9.3 Interest Rate Risk:

Longer-term investments have the potential to achieve higher returns but are also likely to exhibit higher market value volatility due to the changes in the general level of interest rates over the life of the investment. Interest rate risk will be mitigated by providing adequate liquidity for short-term cash needs, and by making longer-term investments only with funds that are not needed for current cash flow purposes. The following strategies will be employed to control and mitigate adverse changes in the market value of the portfolio due to changes in interest rates:

- a) Where feasible and prudent, investment maturities should be matched with expected cash outflows to mitigate market risk.
- b) Investment policy is to invest in securities that are held to maturity. Securities may be sold before maturity in furtherance of the General Objectives of this policy.
- c) To the extent feasible, investment maturities not matched with cash outflows, including liquidity investments under one year, should be staggered to mitigate re-investment risk.
- d) No commitments to buy or sell securities may be made more than 14 days prior to the anticipated settlement date or receive a fee other than interest for future deliveries.
- e) The maximum percent of callable securities in the portfolio shall be 25%;
- f) The maximum stated final maturity of individual securities in the portfolio shall be five years, except as otherwise stated in this policy.
- g) The maximum portfolio average maturity (measured with stated final maturity) shall be 2.0 years.

10. INVESTMENT OF PROCEEDS FROM DEBT ISSUANCE

Investments of bond proceeds are restricted under bond covenants that may be more restrictive than the investment parameters included in this policy. Bond proceeds shall be invested in accordance with the parameters of this policy and the applicable bond covenants and tax laws.

Funds from bond proceeds and amounts held in a bond payment reserve or proceeds fund may be invested pursuant to ORS 294.052. Investments of bond proceeds are typically not invested for resale and are maturity matched with outflows. Consequently, funds within the scope of ORS 294.052 are not subject to this policy's liquidity risk constraints within section 9.2.

Information will be maintained for arbitrage rebate calculations.

11. INVESTMENT OF RESERVE OR CAPITAL IMPROVEMENT FUNDS

Pursuant to ORS 294.135(1)(b), Reserve or Capital Improvement project monies may be invested in securities exceeding five years when the funds in question are being accumulated for an anticipated use that will occur more than 18 months after the funds are invested. With approval of the Board of Water Commissioners, the maturity of the investment or investments made with the funds may occur when the funds are expected to be used.

12. GUIDELINE MEASUREMENT AND ADHERENCE

12.1 Guideline Measurements:

Guideline measurements will use market value investments.

12.2 Guideline compliance:

- a. If the portfolio falls outside of compliance with adopted investment policy guidelines or is being managed inconsistently with this policy, the Investment Officer shall bring the portfolio back into compliance in a prudent manner and as soon as prudently feasible. All violations and recommended actions to bring back into compliance will be reported to the Board of Water Commissioners at the next scheduled meeting.
- b. Due to fluctuations in the aggregate surplus funds balance, maximum percentages for a particular issuer or investment type may be exceeded at a point in time. Securities need not be liquidated to realign the portfolio; however, consideration should be given to this matter when future purchases are made to ensure that appropriate diversification is maintained. Any violations due to aggregate balances will be reported to the Board of Water Commissioners at the next scheduled meeting.
- c. If the credit rating of a properly acquired security is downgraded below the minimum rating level for a new investment in that security, the Investment Officer and Advisor shall evaluate the downgrade on a case-by-case basis in order to determine if the security should be held or sold. The Investment Officer and Advisor will notify the Board of Water Commissioners of the downgrade and their recommended action at the next scheduled meeting.

13. REPORTING AND DISCLOSURE

13.1 Compliance:

The Investment Officer shall prepare a report at least quarterly that allows the Medford Water Commission to ascertain whether investment activities during the reporting period have conformed to the investment policy. The report will include, at a minimum, the following:

- a. A listing of all investments held during the reporting period showing: par/face value, accounting book value, market value, type of investment, issuer, credit ratings, yield to maturity.
- b. Average maturity of the portfolio at period-end.
- c. Maturity distribution of the portfolio at period-end.
- d. Average weighted yield to maturity and yield to worst if callable of portfolio.
- e. Distribution by type of investment.
- f. Transactions since last report.
- g. Distribution of transactions among financial counterparties such as broker/dealers.
- h. Violations of portfolio guidelines or non-compliance issues that occurred during the prior period or that are outstanding. This report should also note actions (taken or planned) to bring the portfolio back into compliance.

13.2 Performance Standards and Evaluation:

The investment officer shall document an investment return comparison of the investment portfolio to a comparative market index. These returns will be provided to the Medford Water Commission at least annually.

When comparing annual performance, all fees and expenses involved with managing the portfolio shall be included in the computation of the portfolio's rate of return.

13.3 Mark to Market:

The market value of the portfolio shall be calculated at least monthly and a statement of the market value of the portfolio shall be reviewed monthly by the Investment Officer.

13.4 Audits:

Management shall establish an annual process of independent review by the external auditor to assure compliance with internal controls. Such audit will include tests deemed appropriate by the auditor.

14. POLICY MAINTENANCE AND CONSIDERATIONS

14.1 Review:

The investment policy shall be reviewed at least annually to ensure its consistency and effectiveness with the overall objectives of preservation of principal, liquidity and return and its compliance with current law. The annual review should also serve as a venue to suggest policies and improvements to the investment program and shall include an investment plan for the coming year.

14.2 Policy Adoption and Amendments:

This investment policy and any modifications to this policy must be adopted by resolution of the Medford Water Commission.

Regardless of whether this policy is submitted to the OSTF Board for comment, this policy shall be re-submitted not less than annually to the Board of Water Commissioners for approval.

15. GLOSSARY OF KEY INVESTMENT TERMS

Accrued Interest. Interest earned but which has not yet been paid or received.

Agency. See "Federal Agency Securities."

Bankers' Acceptance (BA's). A draft or bill of exchange drawn upon and accepted by a bank. Frequently used to finance shipping of international goods. Used as a short-term credit instrument, bankers' acceptances are traded at a discount from face value as a money market instrument in the secondary market on the basis of the credit quality of the guaranteeing bank.

Basis Points. A basis point is a unit of measure used in finance to describe the percentage change in the value or rate of a financial instrument. One basis point is equivalent to 0.01% (1/100th of a percent) or 0.0001 in decimal form. In most cases, it refers to changes in interest rates and bond yields.

Benchmark. A market index used as a comparative basis for measuring the performance of an investment portfolio. A performance benchmark should represent a close correlation to investment guidelines, risk tolerance and duration of the actual portfolio's investments.

Bond Ratings: Corporation's Ability to meet its Financial Obligation

	S&P	Moody's
Extremely Strong Capacity, Highest Quality Minimal Credit Risk	AAA	Aaa
Very Strong Capacity, High Quality Low Credit Risk	AA+	Aa1
	AA	Aa2
	AA-	Aa3
Strong Capacity, Upper Medium Grade Subject to Low Credit Risk	A+	A1
	A	A2
	A-	A3
Weakened Capacity, Medium Grade Subject to Moderate Credit Risk		BBB+ Baa1
	BBB	Baa2
	BBB-	Baa3
Exposure to Adverse conditions, Subject to Substantial Credit Risk		BB+ Ba1
	BB	Ba2
	BB-	Ba3

Broker/Dealer. A person or firm transacting securities business with customers. A "broker" acts as an agent between buyers and sellers and receives a commission for these services. A "dealer" buys and sells financial assets from its own portfolio. A dealer takes risk by owning inventory of securities, whereas a broker merely matches up buyers and sellers. See also "Primary Dealer."

Certificate of Deposit (CD). Bank obligation issued by a financial institution generally offering a fixed rate of return (coupon) for a specified period of time (maturity).

Collateral. Investment securities or other property that a borrower pledges to secure repayment of a loan, secure deposits of public monies, or provide security for a repurchase agreement.

Commercial Paper. Short term unsecured promissory note issued by a company or financial institution. Issued at a discount and matures for par or face value. Usually a maximum maturity of 270 days, and given a short-term debt rating by one or more NRSROs

Corporate Note. A debt instrument issued by a corporation with a maturity of greater than one year and less than ten years.

Counterparty. The other party in a two-party financial transaction. "Counterparty risk" refers to the risk that the other party to a transaction will fail in its related obligations. For example, the bank or broker/dealer in a repurchase agreement.

Current Yield. Annual rate of return on a bond based on its price. Calculated as (coupon rate / price), but does not accurately reflect a bond's true yield level.

Custody. Safekeeping services offered by a bank, financial institution or trust company, referred to as the "custodian." Service normally includes the holding and reporting of the customer's securities, the collection and disbursement of income, securities settlement and market values.

Delivery Versus Payment (DVP). Settlement procedure in which securities are delivered versus payment of cash, but only after cash has been received. Most security transactions, including those through the Fed Securities Wire system and DTC, are done DVP as a protection for both the buyer and seller of securities.

Depository Trust Company (DTC). A firm through which members can use a computer to arrange for securities to be delivered to other members without physical delivery of certificates. A member of the Federal Reserve System and owned mostly by the New York Stock Exchange, the Depository Trust Company uses computerized debit and credit entries. Most corporate securities, commercial paper, CDs and BAs clear through DTC.

Discount Notes. Unsecured general obligations issued by Federal Agencies at a discount. Discount notes mature at par and can range in maturity from overnight to one year. Discount Notes typically have very large primary (new issue) and secondary markets.

Diversification. Dividing investment funds among a variety of security types, maturities, industries and issuers offering potentially independent returns.

Federal Agency Security. A debt instrument issued by one of the federal agencies. Federal agencies are considered second in credit quality and liquidity only to U.S. Treasuries.

Federal Agency. Government sponsored/owned entity created by the U.S. Congress, generally for the purpose of acting as a financial intermediary by borrowing in the marketplace and directing proceeds to specific areas of the economy considered to otherwise have restricted access to credit markets.

Federal Farm Credit Bank (FFCB). A Government Sponsored Enterprise (GSE) system that is a network of cooperatively owned lending institutions that provide credit services to farmers, agricultural cooperatives and rural utilities. The FFCBs act as financial intermediaries that borrow money in the capital markets and use the proceeds to make loans and provide other assistance to farmers and farm-affiliated businesses. Consists of the consolidated operations of the Banks for Cooperatives, Federal Intermediate Credit Banks, and Federal Land Banks. Frequent issuer of discount notes, agency notes and callable agency securities. FFCB debt is not an obligation of, nor is it guaranteed by the U.S. government, although it is considered to have minimal credit risk due to its importance to the U.S. financial system and agricultural industry. Also issues notes under its "designated note" program.

Federal Home Loan Bank System (FHLB). A Government Sponsored Enterprise (GSE) system, consisting of wholesale banks (currently twelve district banks) owned by their member banks, which provides correspondent banking services and credit to various financial institutions, financed by the issuance of securities. The principal purpose of the FHLB is to add liquidity to the mortgage markets. Although FHLB does not directly fund mortgages, it provides a stable supply of credit to thrift institutions that make new mortgage loans. FHLB debt is not an obligation of, nor is it guaranteed by the U.S. government, although it is considered to have minimal credit risk

due to its importance to the U.S. financial system and housing market. Frequent issuer of discount notes, agency notes and callable agency securities. Also issues notes under its “global note” and “TAP” programs.

Federal Home Loan Mortgage Corporation (FHLMC or "Freddie Mac"). One of the large Federal Agencies. A government sponsored public corporation (GSE) that provides stability and assistance to the secondary market for home mortgages by purchasing first mortgages and participation interests financed by the sale of debt and guaranteed mortgage backed securities. FHLMC debt is not an obligation of, nor is it guaranteed by the U.S. government, although it is considered to have minimal credit risk due to its importance to the U.S. financial system and housing market. Frequent issuer of discount notes, agency notes, callable agency securities and MBS. Also issues notes under its “reference note” program.

Federal National Mortgage Association (FNMA or "Fannie Mae"). One of the large Federal Agencies. A government sponsored public corporation (GSE) that provides liquidity to the residential mortgage market by purchasing mortgage loans from lenders, financed by the issuance of debt securities and MBS (pools of mortgages packaged together as a security). FNMA debt is not an obligation of, nor is it guaranteed by the U.S. government, although it is considered to have minimal credit risk due to its importance to the U.S. financial system and housing market. Frequent issuer of discount notes, agency notes, callable agency securities and MBS. Also issues notes under its “benchmark note” program.

Federal Reserve Bank. One of the 12 distinct banks of the Federal Reserve System.

Federal Reserve System (the Fed). The independent central bank system of the United States that establishes and conducts the nation's monetary policy. This is accomplished in three major ways: (1) raising or lowering bank reserve requirements, (2) raising or lowering the target Fed Funds Rate and Discount Rate, and (3) in open market operations by buying and selling government securities. The Federal Reserve System is made up of twelve Federal Reserve District Banks, their branches, and many national and state banks throughout the nation. It is headed by the seven member Board of Governors known as the “Federal Reserve Board” and headed by its Chairman.

Government Sponsored Enterprise (GSE). Privately owned entity subject to federal regulation and supervision, created by the U.S. Congress to reduce the cost of capital for certain borrowing sectors of the economy such as students, farmers, and homeowners. GSEs carry the implicit backing of the U.S. Government, but they are not direct obligations of the U.S. Government. For this reason, these securities will offer a yield premium over Treasuries. Some consider GSEs to be stealth recipients of corporate welfare. Examples of GSEs include: FHLB, FHLMC, FNMA and SLMA.

Government Sponsored Enterprise Security. A security issued by a Government Sponsored Enterprise. Considered Federal Agency Securities.

Index. A compilation of statistical data that tracks changes in the economy or in financial markets.

Investment Advisor. A company that provides professional advice managing portfolios, investment recommendations and/or research in exchange for a management fee.

Liquidity. Relative ease of converting an asset into cash without significant loss of value. Also, a relative measure of cash and near-cash items in a portfolio of assets. Also, a term describing the marketability of a money market security correlating to the narrowness of the spread between the bid and ask prices.

Market Value. The fair market value of a security or commodity. The price at which a willing buyer and seller would pay for a security.

Maturity Date. Date on which principal payment of a financial obligation is to be paid.

Municipal Obligations. A debt instrument issued by a state or local government unit or public agency. The vast majority of municipals are exempt from state and federal income tax, although some non-qualified issues are taxable.

NRSRO. A “Nationally Recognized Statistical Rating Organization.” A designated rating organization that the SEC has deemed a strong national presence in the U.S. NRSROs provide credit ratings on corporate and bank debt issues. Only ratings of a NRSRO may be used for the regulatory purposes of rating such as Moody’s, S&P, Fitch and Duff & Phelps.

Par Value. Face value, stated value or maturity value of a security.

Principal. Face value of a financial instrument on which interest accrues. May be less than par value if some principal has been repaid or retired. For a transaction, principal is par value times price and includes any premium or discount.

Prudent Person Standard. Standard that requires that when investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee will 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. More stringent than the “prudent person” standard as it implies a level of knowledge commensurate with the responsibility at hand.

Rate of Return. Amount of income received from an investment, expressed as a percentage of the amount invested.

Repurchase Agreement (Repo). A short-term investment vehicle where an investor agrees to buy securities from a counterparty and simultaneously agrees to resell the securities back to the counterparty at an agreed upon time and for an agreed upon price. The difference between the purchase price and the sale price represents interest earned on the agreement. In effect, it represents a collateralized loan to the investor, where the securities are the collateral. Can be DVP, where securities are delivered to the investor’s custodial bank, or “tri-party” where the securities are delivered to a third party intermediary. Any type of security can be used as “collateral,” but only some types provide the investor with special bankruptcy protection under the law. Repos should be undertaken only when an appropriate approved master repurchase agreement is in place.

State of Oregon Local Government Investment Pool. The LGIP is organized pursuant to ORS 294.805 through 294.895. Participation in the Pool will not exceed the maximum limit annually set by ORS 294.810.

Safekeeping. Service offered for a fee, usually by financial institutions, for the holding of securities and other valuables. Safekeeping is a component of custody services.

Total Return. Investment performance measured over a period of time that includes coupon interest, interest on interest, and both realized and unrealized gains or losses. Total return includes, therefore, any market value appreciation/depreciation on investments held at period end.

Treasuries. Collective term used to describe debt instruments backed by the U.S. Government and issued through the U.S. Department of the Treasury. Includes Treasury bills, Treasury notes, and Treasury bonds. Also a benchmark term used as a basis by which the yields of non-Treasury securities are compared (e.g., “trading at 50 basis points over Treasuries”).

Treasury Bills (T-Bills). Short-term direct obligations of the United States Government issued with an original term of one year or less. Treasury bills are sold at a discount from face value and do not pay interest before maturity. The difference between the purchase price of the bill and the

maturity value is the interest earned on the bill. Currently, the U.S. Treasury issues 4-week, 13-week and 26-week T-Bills.

Treasury Bonds. Long-term interest-bearing debt securities backed by the U.S. Government and issued with maturities of ten years and longer by the U.S. Department of the Treasury. The Treasury stopped issuing Treasury Bonds in August 2001.

Treasury Notes. Intermediate interest-bearing debt securities backed by the U.S. Government and issued with maturities ranging from one to ten years by the U.S. Department of the Treasury. The Treasury currently issues 2-year, 5-year and 10-year Treasury Notes.

Yield to Maturity (YTM). Calculated return on an investment, assuming all cash flows from the security are reinvested at the same original yield. Can be higher or lower than the coupon rate depending on market rates and whether the security was purchased at a premium or discount. There are different conventions for calculating YTM for various types of securities.