

STAFF REPORT

SUBJECT: Proposed Revisions to San Joaquin Council of Governments' Investment Policy

RECOMMENDED ACTION: By Motion to Adopt Resolution #R-19-13 Approving the San Joaquin Council of Governments' Investment Policy as Revised

DISCUSSION:

RECOMMENDATION:

The San Joaquin Council of Governments, including its roles as the San Joaquin County Transportation Authority and SJCOG, Inc., has an Investment Policy that guides and constrains investment activities of agency funds. The primary funds involved are Measure K revenues and investments related to Measure K and fees paid to SJCOG, Inc. for conservation easements and required endowments. The policy complies with the California State Government Code which provides significant guidance. The Government Code restrictions can be augmented with local policy. This policy is consistent with the Government Code and prudent money management while tailoring investments to the needs of SJCOG.

The standard of prudence to be used by investment officials shall be the "prudent person" standard. The objectives of the Authority's investment activities are, in priority order:

1. Safety. The safety and risk associated with an investment refers to the potential loss of principal and/or interest. SJCOG only enters into those investments that are considered very safe.
2. Liquidity. This refers to the ability to "cash in" at any time with a minimal chance of losing some portion of principal or interest. Liquidity is an important investment quality, especially when the need for unexpected funds may occur.
3. Yield. Yield is the potential dollar earnings an investment can provide, and sometimes is described as the rate of return.

SJCOG's portfolio is invested in five programs:

1. County Pool. With the 2010 Joint Powers Agreement amendment transferring auditor-controller and treasurer functions to the SJCOG Chief Financial Officer,

only Transportation Development Act funds are deposited in the County Treasury pursuant to statute.

2. Local Agency Investment Fund. LAIF is managed by the State Treasurers office and is backed by the full faith and credit of the State of California. LAIF is the repository for hundreds of millions of funds from local agencies throughout the state. LAIF deposits are available within 24 hours.
3. California Asset Management Program. CAMP is a pooled money investment and is responsible for investing Measure K and SJCOG, Inc. revenues. They also invest bond proceeds and track interest earnings for arbitrage and rebate reporting for IRS purposes. The CAMP pool has daily liquidity while providing a competitive yield. CAMP is a joint powers authority comprised of counties, cities, school districts and special districts throughout the state. When the Authority sold bonds in 1993, it became a member of the JPA. CAMP's investment activities are guided and constrained by SJCOG's Investment Policy. (For disclosure purposes, Steve Dial has been the President of CAMP beginning January 1, 2011.)
4. Public Financial Management. PFM manages individual investment portfolios (vis-à-vis the pooled investments) of Measure K sales tax and SJCOG, Inc. portfolios. Using funds that are not going to be needed in the short term, PFM actively buys and sells securities for the Authority and SJCOG, Inc. taking advantage of the first five years of the investment yield curve. PFM is guided and constrained by SJCOG's Investment Policy.
5. Raymond James Financial. In order to capture additional interest yield, Certificates of Deposit have been purchased through Raymond James. The Raymond James portfolio consists of CDs with varying lengths of maturities, however, the portfolio length does not exceed 5 years.

Attached is a memorandum from PFM Asset Management, SJCOG's investment advisor, stating the Investment Policy is in compliance with the sections of the California Government Code (the Code) that governs investment of public funds." PFM does, however, recommend make a few changes to incorporate a recent update to the Code and an update taking effect January 1, 2019. The attached Investment Policy is "redlined" to identify changes to the previously adopted policy. Briefly, the proposed changes are:

Section VIII - Permitted Investment Instruments.

Code change effective January 1, 2017. PFM recommends SJCOG edit some of the credit rating language used in the Policy to reflect a recent revision to the Code. Senate Bill 974, which took effect on January 1, 2017, modified Code Sections 53601 et seq. to clarify that the Code's rating requirements specify the minimum credit rating category required at purchase, without regard to "+", "-", or 1, 2, 3 modifiers.

This Code change simply codified the credit rating interpretation already used by most public agencies, including San Joaquin Council of Governments. This revision did not change the minimum ratings required by the Code for the different investment types. This revision applies to all of the Policy's sections that specify a credit rating requirement for purchase.

SJCOG staff agrees with this recommendation.

Code change effective January 1, 2019. A recent change was made to Code that will go into effect on January 1, 2019 and so we are recommending SJCOG make that change at this time. Governor Jerry Brown recently signed into law changes to the portion of Code referencing mortgage-backed and asset-backed securities. These changes removed the issuer rating requirement and simplified/clarified the security rating requirement.

SJCOG staff agrees with this recommendation.

Section XI: Sales Prior to Maturity

The Policy currently contains specific reporting requirements when a loss on a sale is greater than 1% of principal value of any investment holding. Because losses of greater than 1% are common during a period of sharply rising interest rates, PFM recommends SJCOG review this reporting requirement to determine if this information is useful to SJCOG and if you'd like to continue requiring such reporting. In the attached Policy, this language is highlighted for your review.

SJCOG staff agrees this reporting holds little significance. In many cases the loss for a particular security may be in order purchase a higher yielding note that will ultimately result in greater value.

FISCAL IMPACT:

The Investment Policy provides criteria and guidance for the SJCOG Chief Financial Officer and SJCOG's financial advisors while investing agency funds.

RECOMMENDATION

That the Board adopts resolution R-19-13 adopting the attached Investment Policy for the SJCOG, SJCOG, Inc., and the Transportation Authority.



**RESOLUTION
SAN JOAQUIN COUNCIL OF GOVERNMENTS**

R-19-13

**RESOLUTION OF THE
SAN JOAQUIN COUNCIL OF GOVERNMENTS
ADOPTING AN INVESTMENT POLICY**

WHEREAS, the San Joaquin Council of Governments receives revenues including but not limited to local sales tax under the initiative identified as Measure K, developer fees from SJCOG, Inc.; and

WHEREAS, under law and regulation in the California Government Code, Sections 53600, et. seq., the San Joaquin Council of Governments is required to comply with an investment policy adopted by its policy board and in accordance with the statutes referenced previously; and

WHEREAS, the purpose of the Investment Policy is to identify various policies and procedures that enhance opportunities for a prudent and systematic method of investing and to organize and formalize investment-related activities.

NOW THEREFORE, BE IT RESOLVED that the Board of the San Joaquin Council of Governments adopts the attached Investment Policy to govern the investment-related activities of the agency.

PASSED AND ADOPTED this 6th day of December, 2018 to wit:

AYES:

NOES:

ABSENT:

ROBERT RICKMAN
Chair



November 15, 2018

Memorandum

To: Steve Dial, Deputy Executive Director/CFO
San Joaquin Council of Governments

From: Lauren Brant, Managing Director
Allison Kaune, Senior Managing Director
PFM Asset Management LLC

Re: San Joaquin Council of Governments Investment Policy Review 2018

We completed our review of San Joaquin Council of Governments (“SJCOG”) Investment Policy (the “Policy”) dated October 27, 2016. As written, the Policy is in compliance with the sections of the California Government Code (the “Code”) that govern the investment of public funds. We do, however, recommend that SJCOG make a few changes to the Policy to incorporate a recent update to the Code and an update that will take effect January 1, 2019. We also recommend SJCOG review a requirement of the Policy to ensure it continues to fit your needs. This memorandum explains our recommended revisions to the Policy. We have also attached a marked-up version of the Policy illustrating our recommendations.

Recommendations

Section VIII: Permitted Investment Instruments

Code change effective January 1, 2017. We recommend that SJCOG edit some of the credit rating language used in the Policy to reflect a recent revision to the Code. Senate Bill 974, which took effect on January 1, 2017, modified Code Sections 53601 et seq. to clarify that the Code’s rating requirements specify the minimum credit rating category required at purchase, without regard to “+”, “-”, or 1, 2, 3 modifiers.

This Code change simply codified the credit rating interpretation already used by most public agencies, including San Joaquin Council of Governments. This revision did not change the minimum ratings required by the Code for the different investment types. This revision applies to all of the Policy’s sections that specify a credit rating requirement for purchase.

Code change effective January 1, 2019. A recent change was made to Code that will go into effect on January 1, 2019 and so we are recommending SJCOG make that change at this time. Governor Jerry Brown recently signed into law changes to the portion of Code referencing mortgage-backed and asset-backed securities. These changes removed the issuer rating requirement and simplified/clarified the security rating requirement.

The changes recommended above are shown in the attached Policy.



Section XI: Sales Prior to Maturity

The Policy currently contains specific reporting requirements when a loss on a sale is greater than 1% of principal value of any investment holding. Because losses of greater than 1% are common during a period of sharply rising interest rates, we recommend SJCOG review this reporting requirement to determine if this information is useful to SJCOG and if you'd like to continue requiring such reporting. In the attached Policy, this language is highlighted for your review.

We would be happy to discuss any questions regarding our recommended changes to the Policy.

INVESTMENT POLICY
SAN JOAQUIN COUNCIL OF GOVERNMENTS
October 27, 2016

I. INTRODUCTION

The purpose of this document is to identify various policies and procedures that enhance opportunities for a prudent and systematic investment policy and to organize and formalize investment-related activities.

The investment policies and practices of the San Joaquin Council of Governments (SJCOG), SJCOG Inc. (SJCOGI) and the San Joaquin County Transportation Authority (the Authority) are based on state law and prudent money management. All funds will be invested in accordance with the Authority's Investment Policy, and California Government Code Sections 53600 et. seq. The investment of bond proceeds will be governed by the provisions of relevant bond documents.

II. SCOPE

It is intended that this policy cover all funds (except retirement funds and bond proceeds) and investment activities under the direction of SJCOG, SJCOGI and the Authority.

III. PRUDENCE

Section 53600.3 of the Government Code identifies as trustees those persons authorized to make investment decisions on behalf of a local agency. As a trustee, the standard of prudence shall be the "prudent investor" standard. When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency.

Investment officers acting in accordance with written procedures and the investment policy and exercising due diligence shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments.

IV. OBJECTIVES

The primary objectives, in priority order, of the SJCOG, SJCOGI and Authority's investment activities shall be:

- 1) Safety. Safety of principal is the foremost objective of the investment program. The SJCOG, SJCOGI and Authority's investments shall be undertaken in a manner that seeks to ensure preservation of capital in the portfolio. The objective will be to mitigate credit risk and interest rate risk.
 - a) Credit Risk: The SJCOG, SJCOGI, and the Authority will minimize credit risk, which is the risk of loss due to the failure of the security issuer or backer, by:
 - Limiting investments to the types of securities listed in the Permitted Investment Instruments Section of this Investment Policy.
 - Diversifying the investment portfolio so that the impact of potential losses from any one type of security or from any one individual issuer will be minimized.
 - b) Interest Rate Risk: The SJCOG, SJCOGI, and the Authority will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by:
 - Structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity.
- 2) Liquidity. The SJCOG, SJCOGI and Authority's investment portfolio will remain sufficiently liquid to enable the Authority to meet its cash flow requirements.
- 3) Return on Investment. The SJCOG, SJCOGI and Authority's investment portfolio shall be designed with the objective of attaining a market rate of return on its investments consistent with the constraints imposed by its safety objective and cash flow considerations.

V. DELEGATION OF AUTHORITY

The management responsibility for the investment program is hereby delegated to the Deputy Executive Director/Chief Financial Officer who shall monitor and review all investments for consistency with this investment policy. No person may engage in an investment transaction except as provided under the limits of this policy. The Authority may delegate its investment decision-making and execution authority to an investment advisor. The advisor shall follow the policy and such other written instructions as are provided.

Delegation of authority is valid for one year and is good until the delegation expires or is revoked by action of the Board.

VI. ETHICS AND CONFLICT OF INTEREST

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

VII. INTERNAL CONTROLS

The Authority shall establish a set of internal controls that can be documented in writing (Exhibit A). SJCOG, SJCOGI, and the Authority and the external independent auditor will review the internal controls. The controls shall be designed to prevent employee error, misrepresentations by third parties, unanticipated changes in financial markets, or imprudent actions by officers or employees of SJCOG, SJCOGI and the Authority.

VIII. PERMITTED INVESTMENT INSTRUMENTS

1. United States Treasury notes, bonds, bills, or certificates of indebtedness, or those for which the faith and credit of the United States are pledged for the payment of principal and interest.
2. 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 of United States government-sponsored enterprises.
3. Repurchase Agreements used solely as short-term investments not to exceed one year.

SJCOG, SJCOGI and the Authority may enter in Repurchase Agreements with primary dealers in U.S. Government securities who are eligible to transact business with, and who report to, the Federal Reserve Bank of New York.

The following collateral restrictions will be observed: Only U.S. Treasury securities or Federal Agency securities, as described in VIII, 1 and 2, will be acceptable collateral. All securities underlying Repurchase Agreements must be delivered to SJCOG, SJCOGI and the Authority's custodian bank by book entry, physical delivery, or by a third party custodial agreement. The total market value of all collateral for each Repurchase Agreement must equal or exceed, on the basis of market value, 102 percent of the total dollar

value of the money invested by SJCOG, SJCOGI and the Authority for the term of the investment. For any Repurchase Agreement with a term of more than one day, the value of the underlying securities must be calculated at least weekly.

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

SJCOG, SJCOGI and the Authority or its trustee shall have a perfected first security interest under the Uniform Commercial Code in all securities subject to Repurchase Agreement.

SJCOG, SJCOGI and the Authority will have properly executed a PSA agreement with each counter party with which it enters into Repurchase Agreements.

4. Reverse repurchase agreements may be used only after prior approval of SJCOG, SJCOGI and the Authority's Board of Directors. If a reverse repurchase agreement is authorized, it may be utilized only if the security to be sold on reverse repurchase agreement has been owned and fully paid for by SJCOG, SJCOGI and the Authority for a minimum of 30 days prior to the sale; the total of all reverse repurchase agreements on investments owned by SJCOG, SJCOGI and the Authority does not exceed 20 percent of the base value of the portfolio; and the agreement does not exceed a term of 92 days, unless the agreement includes a written codicil guaranteeing a minimum earning or spread for the entire period between the sale of the security using a reverse repurchase agreement and the final maturity date of the same security. The proceeds of the Reverse Repurchase Agreement may not be invested in securities whose maturity exceeds the term of the Reverse Repurchase Agreement.
5. Registered treasury notes or bonds of this or any of the other 49 United States, 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 or any of the other 49 United States.
6. Bonds, notes, warrants, or other evidences of indebtedness of any local agency within this state, 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.
7. Bankers' Acceptances otherwise known as bills of exchange or time drafts

that are drawn on and accepted by a commercial bank, the short-term paper of which is rated in the highest category by a nationally recognized statistical-rating organization.

Purchases of Banker's Acceptances may not exceed 180 days maturity or 40 percent of the Authority's surplus money. No more than 30 percent of SJCOG, SJCOGI and the Authority's surplus funds may be invested in the Banker's Acceptances of any one commercial bank.

8. Commercial paper of "prime" quality of the highest ranking or of the highest letter and number rating, as provided by a nationally recognized statistical-rating organization. The entity that issues the commercial paper shall meet all of the following conditions in either paragraph (A) or paragraph (B):

- (A) 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 in a rating category of "A" or its equivalent or higher by a nationally recognized statistical-rating organization.

- (B) 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 nationally recognized statistical-rating organization.

Purchases of eligible commercial paper may not exceed 270 days maturity nor represent more than 10 percent of the outstanding paper of an issuing corporation.

Purchase of commercial paper may not exceed 25 percent of SJCOG, SJCOGI and the Authority's surplus money that may be invested. No more than 5 percent of the Authority's investment portfolio may be invested in any one commercial paper issuer.

9. Medium-term corporate notes, defined as all corporate and depository institution debt securities issued by corporations organized and operating within the United States or by depository institutions licensed by the U.S. or any state and operating within the U.S. Medium-term corporate notes shall be rated in a rating category of "A" or its equivalent or better by a

nationally recognized statistical-rating organization.

Purchases of medium-term corporate notes may not exceed 30 percent of SJCOG, SJCOGI and the Authority's surplus money. No more than 5 percent of the Authority's investment portfolio may be invested in any one medium-term note issuer.

10. FDIC insured or fully collateralized time certificates of deposit in a state or national bank, savings association or federal association, federal or state credit union located in California, including U.S. branches of foreign banks licensed to do business in California

To be eligible to receive local agency deposits, a financial institution must have received a minimum overall satisfactory rating for meeting the credit needs of California Communities in its most recent evaluation.

11. Negotiable certificates of deposit issued by a nationally or state-chartered bank, a savings association or a federal association, a state or federal credit union, or by a federally licensed or state-licensed branch of a foreign bank.

Purchase of negotiable certificates of deposit may not exceed 30 percent of SJCOG, SJCOGI and the Authority's surplus money. No more than 5 percent of the Authority's investment portfolio may be invested in any one negotiable CD issuer.

The legislative body of a local agency and the treasurer or other official of the local agency having legal custody of the moneys are prohibited from investing local agency funds, or funds in the custody of the local agency, in negotiable certificates of deposit issued by a state or federal credit union if a member of the legislative body of the local agency, or a person with investment decision making authority in the administrative office manager's office, budget office, auditor-controller's office, or treasurer's office of the local agency also serves on the board of directors, or any committee appointed by the board of directors, or the credit committee or the supervisory committee of the state or federal credit union issuing the negotiable certificates of deposit.

12. State of California's Local Agency Investment Fund

The LAIF portfolio should be reviewed periodically. The maximum balance that can be held in the fund is the maximum amount permitted by the Local Investment Advisory Board.

13. Insured savings account or money market account.

To be eligible to receive local agency deposits, a financial institution must have received a minimum overall satisfactory rating for meeting the credit needs of California Communities in its most recent evaluation.

14. Shares of beneficial interest issued by a joint powers authority organized pursuant to Government Code Section 6509.7 that invests in the securities and obligations authorized in Government Code Section 53601 subdivisions (a) to (q), inclusive. Each share shall represent an equal proportional interest in the underlying pool of securities owned by the joint powers authority. To be eligible under this section, the joint powers authority issuing the shares shall have retained an investment adviser that meets all of the following criteria:

- (1) The adviser is registered or exempt from registration with the Securities and Exchange Commission.

- (2) The adviser has not less than five years of experience investing in the securities and obligations authorized in subdivisions (a) to (q), inclusive.

- (3) The adviser has assets under management in excess of five hundred million dollars (\$500,000,000).

15. 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. To be eligible for investment pursuant to this subdivision these companies must:

- (1) Attain the highest ranking or highest letter and numerical rating provided by not less than two nationally recognized statistical rating services

- (2) Have an investment advisor registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience managing money market mutual funds with assets under management in excess of five hundred million dollars (\$500,000,000).

The purchase price of shares of beneficial interest purchased shall not include any commission that these companies may charge and shall not exceed 20 percent of SJCOG, SJCOGI and the Authority's surplus money that may be invested pursuant to 53601 of the California Government Code

16. Asset Backed Securities, defined as all mortgage pass-through securities, collateralized mortgage obligations, mortgage-backed or other pay-through bonds, equipment lease-backed certificates, consumer receivable pass-through certificates, and consumer receivable-backed bonds, with a maximum remaining maturity of five years or less.

Asset backed securities shall be rated in a rating category of “AA” or its equivalent or better by a NRSRO.

Purchase of asset backed securities may not exceed 20 percent of the Authority’s investment portfolio. No more than 5 percent of the Authority’s investment portfolio may be invested in asset backed securities of any one issuer.

17. Supranationals, defined as United States dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank, with a maximum remaining maturity of five years or less, and eligible for purchase and sale within the United States. Supranationals shall be rated in a rating category of “AA” or its equivalent or better by a NRSRO.

Purchase of Supranationals may not exceed 30 percent of the Authority’s investment portfolio.

The security type and issuer percentage limitations listed in this section refer to the allocation of the Authority’s investment portfolio at the time the security is purchased. Credit criteria listed in this section refers to the credit of the issuing organization at the time the security is purchased. If a credit rating falls below the criteria stated, SJCOG, SJCOGI and the Authority shall be notified. Maximum percentage limitations also apply at the time of purchase.

IX. INELIGIBLE INVESTMENTS

SJCOG, SJCOGI and the Authority shall not invest any funds in inverse floaters, range notes, or interest-only strips that are derived from a pool of mortgages, or in any security that could result in zero interest accrual if held to maturity.

X. MAXIMUM MATURITY

Investment maturities shall be based on a review of cash flow forecasts. Maturities will be scheduled so as to permit SJCOG, SJCOGI and the Authority to meet all projected obligations.

The maximum maturity will be no more than five years from purchase date to maturity date, unless the legislative body has granted express authority to make that investment either specifically or as a part of an investment program approved by the legislative body no less than three months prior to the investment.

XI. SALES PRIOR TO MATURITY

Securities shall not be purchased for the specific purpose of trading. However, sales prior to maturity are permitted under the following circumstances: (1) to meet an unanticipated disbursement, or (2) reinvesting the proceeds to improve the quality, yield, return or target duration in the portfolio. Certain opportunities may involve the recognition of value losses. Book value trading losses are permitted. Any trading loss greater than 1% of principal value of any investment holding requires the following: (1) explanation of source of loss, (2) rationale for transactions resulting in recognition of loss, (3) estimation of time necessary to recoup the loss.

XII. REPORTING REQUIREMENTS

The Deputy Executive Director/Chief Financial Officer shall render to the Executive Director and the Board of Directors an investment report each quarter, which shall include, at a minimum, the following information for each individual investment:

- Type of investment instrument
- Issuer name
- Purchase date
- Maturity date
- Purchase price
- Par Value
- Current market value and the source of the valuation
- Overall portfolio yield based on cost
- Sale Date of any investment sold prior to maturity

The quarterly report also shall (i) include a monthly list of transactions, (ii) state compliance of the portfolio to the statement of investment policy, or manner in which the portfolio is not in compliance, (iii) include a description of any of SJCOG, SJCOGI and the Authority's funds, investments or programs that are under the management of contracted parties, including lending programs, and (iv) include a statement denoting the ability of SJCOG, SJCOGI and the Authority to meet its expenditure requirements for the next six months, or provide an explanation as to why sufficient money shall, or may, not be available.

This quarterly report shall be submitted within 30 days following the end of the quarter.

The Deputy Executive Director/Chief Financial Officer shall annually render to the Board a statement of investment policy, which the Board shall consider at a public meeting.

XIII. SAFEKEEPING AND CUSTODY

All security transactions, including collateral for repurchase agreements, shall be executed by delivery vs. payment (DVP). This means that the securities shall be delivered to SJCOG, SJCOGI and the Authority or their designated custodian upon receipt of payment. The only exception to the foregoing shall be depository accounts and securities purchases made with: (i) local government investment pools; (ii) time certificates of deposit, and, (iii) money market mutual funds, since the purchased securities are not deliverable. Evidence of each these investments will be held by the Deputy Executive Director/Chief Financial Officer.

All securities that may be purchased, including collateral for repurchase agreements, shall be held by a third party custodian designated by SJCOG, SJCOGI, and the Authority. These securities shall be held in the entity's name and control and third party custody shall be evidenced by safekeeping receipts. The third party custodian shall send SJCOG, SJCOGI, and the Authority, on a monthly basis, a statement of what is safekept and this statement shall be reconciled on a monthly basis. Securities held in custody for SJCOG, SJCOGI, and the Authority shall be independently audited on an annual basis to verify investment holdings.

APPENDIX A
INVESTMENT PROCEDURES
INTERNAL CONTROL GUIDELINES
SEGREGATION OF RESPONSIBILITIES OF THE SJCOG FINANCE FUNCTIONS

The following internal control guidelines are a segregation of responsibilities of SJCOG finance functions and have been adapted from information provided by the California Municipal Treasurers Association, in cooperation with the California Municipal Finance Officers Association and the County Treasurers Association.

Objectives of Internal Control

Internal control is the plan of this organization and all the related systems established by management's objective of ensuring, as far as practicable:

- The orderly and efficient conduct of its business, including adherence to management policies,
- The safeguarding of assets,
- The prevention and detection of errors and fraud,
- The accuracy and completeness of the accounting records, and
- The timely preparation of reliable financial information.

Limitations of Internal Control

No internal control system, however elaborate, can, by itself, guarantee the achievement of management's objectives. Internal control can provide only reasonable assurance that the objectives are met, because of its inherent limitations, including:

- Management's usual requirement that a control be cost effective.
- The direction of most controls are recurring, rather than unusual types of transactions.
- Human error due to misunderstanding, carelessness, fatigue or distraction.
- Potential for collusion that circumvents controls dependent on segregation of functions.
- Potential for a person responsible for exercising control abusing that responsibility; a member of management is frequently in a position to override controls which management has set up.

Elements of Internal Control

Elements of a system of internal control are the means by which an organization can satisfy the objectives of internal control. The elements are:

1. Organization

Specific responsibility for the performance of duties should be assigned and lines of authority and reporting clearly identified and understood.

2. Personnel

Personnel should have capabilities commensurate with their responsibilities. Personnel selection and training policies together with the quality of supervision are thus important.

3. Segregation of Functions

Segregation of incompatible functions reduces the risk that a person is in a position both to perpetrate and conceal errors or fraud in the normal course of duty. If two parts of a transaction are handled by different people, collusion is necessary to conceal errors or fraud. In particular, the functions that should be considered when evaluating segregation of functions are authorization, execution, recording, custody of assets, and performing reconciliations.

4. Authorization

All transactions should be authorized by an appropriate responsible individual. The responsibilities and limits of authorization should be clearly delineated. The individual or group authorizing a specific transaction or granting general authority for transactions should be in a position commensurate with the nature and significance of the transactions. Delegation of authority to authorize transactions should be handled very carefully.

5. Controls Over an Accounting System

Controls over an accounting system include the procedures, both manual and electronic, carried out independently to ascertain that recorded transactions are complete, valid, authorized, and properly recorded.

6. Safeguarding of Assets and Records

Controls should be in place to prevent and detect loss, theft or deterioration of assets. In addition, safeguards are necessary to prevent the loss or destruction of records and documentation. These controls would involve custodial controls, which are designed to prevent or detect unauthorized access to or use of assets and records, and accountability controls, which compare accounting records to determine where recorded assets exist and are properly recorded, in accordance with generally accepted accounting principles (GAAP).

7. Management

These are the controls exercised by management including day-to-day supervision, overall supervisory controls, management review of budgets, management review of the adequacy of internal control, and the internal audit function.

Segregation of Responsibilities of the SJCOG Finance Functions

1. Authorization of investment transactions:

- Formal investment policy should be:

a) prepared by	Chief Financial Officer
b) submitted to	Executive Director & SJCOG Board

- Investment transactions should be approved by Chief Financial Officer

2. Execution of investment transactions Investment Advisor

3. Timely recording of investment transactions:

- Recording of investment transactions in the accounting records Chief Accountant

Segregation of Responsibilities of the SJCOG Finance Functions

1. Verification of investment, i.e., match broker confirmation to SJCOG's records Chief Accountant

2. Safeguarding of assets and records:

- | | | |
|----|---|---|
| - | Reconciliation of SJCOG's records to the accounting records | Accounting Assistants |
| - | Reconciliation of Treasurer's records to bank statements and safekeeping records | Accounting Assistants |
| - | Review of: | |
| | a) Financial institution's financial condition | Investment Advisor and Chief Financial Officer |
| | b) Safety, Liquidity, and potential yields of investment instruments, and | Investment Advisor and Chief Financial Officer
Chief Financial Officer |
| | c) Reputation and financial condition of investment brokers/dealers | Investment Advisor and Chief Financial Officer |
| | d) Periodic reviews of collateral should be performed | Chief Financial Officer |
| - | Investment securities shall be safe-kept unless there are adequate controls limiting unauthorized access. Whenever possible, investment securities shall be held in safekeeping by the SJCOG's designated third party custodian. | Trust Department |
| 6. | Management's periodic review of the investment portfolio as prepared by the Investment Advisor-key areas which should be reviewed are investment types, purchase price, market values, maturity dates and investment yields, as well as, conformance to stated investment policy. | Chief Financial Officer, Independent Auditors (external) |