Board Policy No. 349

Investment Policy

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Section 1.0 Investment Policy Statement

It is the policy of the District to invest all public funds in accordance with the following goals, listed in descending order of priority:

A. Compliance with all applicable laws, statutes, ordinances, and regulation requirements.
B. Preservation of capital.
C. Liquidity to meet required cash demands.
D. Maximization of income.

Section 2.0 Investment Policies

This investment policy applies to the investment activities of the Alameda Contra Costa Transit District. The financial assets of all District funds shall be administered in accordance with the provisions of this policy, except for Section 457 Deferred Compensation Plan funds, which shall be invested in accordance with the applicable laws, regulations, and contracts for such funds.

Funds of the Alameda Contra Costa Transit District Pension Fund are not subject to this policy as the Pension Fund is administered by the Alameda Contra Costa Transit District Retirement Board, a separate entity from the District.

Section 3.0 Accounting Policies

Short-term investments (those with a remaining maturity at the time of purchase of one year or less) are reported at cost, which approximates fair value, provided that the fair value of those investments is not significantly affected by the impairment of the credit standing of the issuer or by other factors.

Investments with a remaining maturity at the time of purchase of greater than one year are carried at fair value. For financial reporting purposes, all investment income, including changes in fair value of investments, is recognized as revenue in the District's operating statement.

Section 4.0 Prudence (Prudent Person Rule)

District investments shall be made with care, skill, prudence and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the District.

Persons acting in accordance with this 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 the monthly investment report to the District Board, and appropriate action is immediately taken to control adverse developments.

Section 5.0 Objectives

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

A. With respect to **all** investments:

1. To be in compliance with all Federal, State and local laws as well as all District policies and procedures.

2. To ensure safety of principal. All investments of the District shall be undertaken in a manner which seeks the preservation of principal.

3. To remain sufficiently liquid to enable the District to meet all operating requirements which might be reasonably anticipated.

4. To maximize yield consistent with risk limitations identified herein and prudent investment principles.

B. With respect to short-term Cash Management objectives:

1. To accelerate receipt of all funds due the District.

2. To accurately monitor and forecast expenditures and revenues, thus enabling the District to invest funds to the fullest extent possible.

3. The investment portfolio shall be designed with the objective of obtaining a rate of return throughout budgetary and economic cycles, commensurate with the investment risk constraints and the cash flow needs. The basis used by the Director of Revenue Management to determine whether market yields are being achieved shall be the three (3) month U.S. Treasury Bill and the average Federal Funds rate. This index is considered a benchmark for "riskless" investment transactions and therefore should be a minimum standard for the portfolio's rate of return.

Section 6.0 Delegation of Authority

The following individuals are authorized to sign investment documents and/or execute cash transfers and make investments of the District's funds:

A. General Manager
B. Chief Financial Officer
C. Director of Revenue Management or Treasury Services Administrator

All investment documents and cash transfer authorization forms shall be approved by (2) signature authorities from the above list. In the exercise of this responsibility, the authority to perform specific investment tasks and duties may be delegated as follows:

> **Controller:** If the General Manager or Chief Financial Officer are out of the office for any reason, the Controller may sign and execute the necessary investment documents and cash transfer authorization forms as the 2nd signature authority.

Section 7.0 Ethics and Conflicts Of Interest

The officers and authorized employees as defined in Section 6.0 of this policy who are responsible for the investment of District funds shall refrain from personal business activity that could conflict with the proper execution of the District's investment program, or which could impair the ability to make impartial investment decisions.

Pursuant to the District's Conflict of Interest Code, employees shall disclose any financial interests in financial institutions that conduct business within the District. They shall further disclose any personal financial/investment holdings that could affect the performance of the District's portfolio or the individual's judgement or decisions regarding the District's portfolio.

In addition, the services provided by the District's external auditors shall include an annual review of the Fair Political Practices Commission "Statement of Economic Interests, Form 700", for individuals authorized to make investments of District funds. As outlined in Section 6.0 of this policy, those individuals are:

A. General Manager
B. Chief Financial Officer
C. Director of Revenue Management
D. Treasury Services Administrator

Section 8.0 Authorized Financial Dealers and Institutions

The Director of Revenue Management shall maintain a list of authorized dealers and financial institutions that have total capital in excess of $1 billion, are members of SIPC (Securities Investor Protection Corporation), and are in compliance with the Securities Exchange Commission's rule 15C3-1 (uniform net capital rule). In conformance with the District Investment Policy, only those entities listed will be considered as a viable dealer to provide investment services to the District.

All financial institutions and broker/dealers who desire to become qualified bidders for investment transactions must supply the following: 1) audited financial statements; 2) proof of National Association of Security Dealers (NASD) certification; 3) certification of having read our investment policy and agreement to comply with the policy requirements.

No public deposit shall be made except in a qualified public depository as established by Government Code Section 53635.2.

Section 9.0 Authorized and Suitable Investments

In accordance with and subject to the restrictions in California Government Code Section 53601, the District may invest in the following types of investments:

A. Repurchase Agreements
B. Securities of U.S. Government and its agencies
C. California Local Agency Investment Fund (LAIF)
D. Negotiable Certificates of Deposit
E. Commercial Paper
F. Bankers Acceptances
G. Money Market Accounts (Non U.S. Gov't)

Although Local Agency Investment Funds, Negotiable Certificates of Deposit, Commercial Paper, and Bankers Acceptances, are allowed under the California Government Code, these types of investments may not be utilized without the prior authorization of the Chief Financial Officer, after prudent investigation of the credit risk of such investments.

Section 10.0 Collateralization

California banks and savings and loan associations are required to secure District deposits by pledging eligible securities as collateral, pursuant to California Government Code Section 53651. In accordance with California Government Code Section 53652, the fair value of the pledged securities must equal at least 110 percent of the District's deposits. California law also allows financial institutions to secure deposits by pledging first trust deed mortgage notes having a value of 150 percent of the District's total deposits.

Pursuant to California Government Code Section 53601, the fair value of securities that underlay a repurchase agreement shall be valued at 102 percent or greater of the funds borrowed against those securities and the value shall be adjusted no less than quarterly.

As a matter of District policy, all deposits of the District are secured by the pledge of eligible securities equal to 110 percent of the District's deposits. All repurchase agreement transactions of the District must meet the requirements in California Government Code Section 53601 and shall be secured by the pledge of eligible securities equal to 102 percent of the District's principal investment.

In accordance with California Government Code 53653, the District Director of Revenue Management may waive the 110 percent collateral requirement for deposits which are insured up to $250,000 by the FDIC.

Section 11.0 Safekeeping and Custody

Securities purchased as District investments must be physically delivered to a third-party agent of the District. If U.S. Treasury securities are purchased, delivery may be made by book entry only. All investment transactions for the District require "Delivery vs. Payment" method of settlement only.

The District's securities and collateral for those securities shall be maintained, in the name of the District, in the Trust Department or Safekeeping Department of the various banks doing business with the District as established by written third-party safekeeping agreements between the District and the banks.

Section 12.0 Diversification

The District shall diversify its investments by security type, institution and maturity. With the exception of securities of the U.S. Government and its Agencies, no more than 33% of the District's total investment portfolio shall be invested in a single security type or with a single financial institution.

Section 13.0 Maximum Maturities

To the extent possible, the District shall match its General Fund investments with anticipated cashflow requirements. Unless matched to a specific cashflow, the District shall not directly invest in maturities greater than **3 years** from the date of purchase without prior authorization of the Board of Directors.

All investments of District funds shall be made in accordance with and subject to the restrictions in California Government Code Section 53601. Short term investment of District funds shall be restricted to the following instruments:

Investment Instruments	Maximum Percentage/ Amt$ of Portfolio	Maximum Length to Maturity for Short Term Investments
Repurchase Agreements*	$25M	7 days
U.S. Treasury Bills & Notes	100%	3 years
U.S. Government Agency Securities	100%	3 years
Bankers Acceptances	20%	180 days
Commercial Paper	20%	270 days
Local Agency Investment Funds	20%	n/a
Negotiable Cert. of Deposit	20%	3 years
Money Market Accounts (Non U.S. Gov't)	$25M	n/a
Interest Bearing Cash Collateralized by Securities of the U.S. Government or Its Agencies	100%	

*All repurchase agreements entered into by the District require that an authorized master repurchase agreement between the District and the financial institution be in place before any repurchase agreement transactions occur.

Section 14.0 Internal Controls

The Director of Revenue Management shall establish a system of internal controls through procedures designed to prevent losses of public funds arising from fraud, employee error, misrepresentation of third parties, unanticipated changes in financial markets, or imprudent actions by employees and officers of the District. These controls shall include:

A. Development of investment procedures inclusive of but not limited to:

1. Separation of transaction authority from accounting and record keeping responsibilities.

2. Third-Party safekeeping of securities.

3. Competitive bids shall be obtained only from authorized dealers and financial institutions, as described in Section 8.0 of this policy.

4. All investments shall be selected through an informal documented competitive telephone bid process. If a specific maturity date is required, bids will be requested from at least three "authorized dealers and financial institutions" for instruments which meet the maturity requirement. If no specific maturity is required, a yield curve analysis will be conducted to determine which maturities produce the greatest yield prior to securing the required competitive bids described above.

5. Written confirmation of all financial transactions.

6. Written documentation of bids, transactions and investment strategies.

B. Periodic independent reviews to be conducted to ensure the District's investment operation is in compliance with the established policy and associated procedures.

C. The investment portfolio and all related transactions are reviewed and balanced to appropriate general ledger accounts by the Controller's office on a monthly basis.

Section 15.0 Reporting Requirements

The Director of Revenue Management shall be responsible for preparing a monthly investment report as required by California Government Section 53607. The investment report shall include:

A. Type of Investment
B. Institution of Purchase
C. Date of Purchase, and Maturity
D. Interest Rate, Rate of Return, and Yield

E. Target Benchmark
F. Par, Book and Fair Values

In addition, the investment report shall state compliance of the portfolio with the statement of investment policy and a statement denoting the ability of the District to meet pool expenditure requirements for the next 6 months in accordance with California Government Section 53646 (b) (2) and (3).

The investment report is to be produced monthly and will be forwarded to the Finance and Audit Committee and then to the full Board of Directors for review.

Section 16.0 Fuel Hedging Program

Staff is directed to utilize appropriate fuel hedging strategy to minimize the variability in the District's budget due to fluctuations in the price of diesel fuel. This variability is due to the fact that the District primarily purchases fuel on the spot market, which varies daily and may subject the District to volatile variances between budgeted and actual fuel expense. Variances between budgeted and actual fuel expenses vary significantly during any given year. The hedging program is designed to minimize large budget variances resulting from the volatility of diesel fuel prices. Hedging increases budget certainty and facilitates more effective utilization of budgetary resources. The District's hedging program will include:

A. Fixed price Physical Delivery Contracts

   Subject to an open and competitive process, the District solicits bid prices and award contracts for future delivery of fuel from suppliers.

B. Fuel Commodity Swap

   The District enters into a financially-settling contract with qualifying counterparties under which the District either pays an upfront amount or exchanges future payments with a counterparty.

C. Futures Contracts

   The District may enter into such contracts that allow it to enter into smaller transactions and make certain pricing decisions over time.

<u>Risks</u>

Any strategy to fix or otherwise hedge future prices carries certain risks, some of which are identified below. Certain of these risks may be mitigated, in part, by taking certain measures, some of which are also identified below.

Counterparty Risk: The risk that the counterparty fails to make required payments or otherwise comply with the terms of the hedging contract. This non-performance would expect to result from financial difficulty, but also may occur for physical, legal or business reasons. This risk is mitigated by establishing minimum credit quality criteria, establishing maximum credit limits, requiring collateral upon a counterparty downgrade and when credit limits are exceeded, limiting the term of the agreement and employing credit rating surveillance.

Pricing Risk: The risk that, during the term of the hedging contract, the District usually pays a higher price than it would have paid by purchasing diesel fuel in the spot market alone, without entering into a hedging contract.

Political Risk: The risk that the hedging program may be unjustly criticized. Political risk is mitigated by ensuring that the Board and public are fully informed about the purpose, nature and expectations for the hedging program.

Basis Risk: The risk that there is a mismatch between any payment received from a counterparty and the variable cost for diesel fuel actually paid to a gas company. . Such basis risk may be mitigated by basing hedging contracts on indices that have a strong historical correlation with the price of diesel fuel in the relevant market.

Termination Risk: The risk that there will be an early termination of a hedging contract. An early termination may result in the District either paying or receiving a termination payment. Early termination may result in the District either paying or receiving a termination payment. Early terminations generally occur when one of the parties deteriorates in credit quality, suffers bankruptcy or fails to perform. The risk is mitigated by establishing safeguards such as requiring collateral posting if credit limits are exceeded or credit ratings decline.

Fuel Commodity Transactions

Each Fuel Commodity Transaction shall have a term not to exceed the Maximum Term and shall be for a notional quantity of diesel fuel not to exceed the Maximum Percentage. Further, each Fuel Commodity Transaction shall be entered into solely with a Fuel Hedge Counterparty under a Fuel Hedge Agreement and shall contain a Fuel Hedge Collateral Provision and a Fuel Hedge Termination Provision. Each Fuel Commodity Transaction shall include a provision that permits the District to early terminate such transaction at any time and for any reason, at its option.

Each contemplated Fuel Commodity Transaction shall be approved by the Board prior to the Staff entering into such transaction. Subject to any additional parameters established by the Board in its approval, the Staff shall be permitted to award a Fuel Commodity Transaction to any qualifying Fuel Hedge Counterparty bidding on such transaction after evaluating the price quoted, credit quality and reputation of each bidding Fuel Hedge Counterparty, and any other information it may deem relevant or appropriate. Each Fuel Hedge Counterparty shall enter into a Fuel Hedge Agreement prior to or promptly following the execution of a Fuel Commodity Transaction.

The Staff shall monitor, on a continuing basis during the existence of a Fuel Commodity Transaction, the index upon which any Fuel Commodity Transaction is based and the credit ratings of each Fuel Hedge Counterparty. On a quarterly basis following the execution of a Fuel Commodity Transaction, the Staff shall deliver a report to the Board regarding such Fuel Commodity Transaction, including the existence of any significant events or occurrences under the Fuel Hedge Agreement, any operational or other issues relating to the management of such transaction and the overall economic performance of such transaction. The Staff shall report to the Board the occurrence of any default or termination event, however described, with respect to a Fuel Hedge Counterparty under a Fuel Hedge Agreement or the downgrade of any Fuel Hedge Counterparty immediately upon becoming aware of any such event or occurrence.

Section 17.0 Investment Policy Adoption

The District's investment policy shall be adopted by resolution of the District's Board of Directors. This policy shall be reviewed on an annual basis by the Board of Directors. Any modifications made thereto must be formally approved by the Board of Directors.

Section 18.0 Glossary

ACCRUED INTEREST: The accumulated interest due on a bond as of the last interest payment made by the issuer.

AGENCY: A debt security issued by a federal or federally sponsored agency. Federal agencies are backed by the full faith and credit of the U.S. Government. Federally sponsored agencies are backed by each particular agency with a market perception that there is an implicit government guarantee. An example of a federal agency is the Government National Mortgage Association (GNMA). An example of a FSA is the Federal National Mortgage Association (FNMA).

AMORTIZATION: The systematic reduction of the amount owed on a debt issued through periodic payments of principal.

BASIS POINT: A unit of measure used in the valuation of fixed-income securities equal to 1/100 of 1 percent of yield, e.g., "1/4" of 1 percent is equal to 25 basis points.

BID: The price offered for securities.

BROKER: A broker brings buyers and sellers together for a commission paid by the initiator of the transaction or by both sides. In the money market, brokers are active in markets in which banks buy and sell money and in interdealer markets.

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: An unsecured short-term promissory note issued by corporations, with maturities ranging from 2 to 270 days.

COUPON: The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value; 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, including buying and selling for his/her own account.

DELIVERY VERSUS PAYMENT: There are two methods of delivery of securities: delivery versus payment and delivery versus receipt (also called free). 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 amount by which the par value of a security exceeds the price paid for the security.

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

FAIR VALUE: The amount at which an investment could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

FEDERAL FUNDS (FED FUNDS): Funds placed in Federal Reserve banks by depository institutions in excess of current reserve requirements. These depository institutions may lend fed funds to each other overnight or on a longer basis. They may also transfer funds among each other on a same-day basis through the Federal Reserve banking systems. Fed funds are considered to be immediately available funds.

FEDERAL FUNDS RATE: Interest rate charged by one institution lending federal funds to the other.

FUEL COMMODITY TRANSACTIONS: A financially-settling diesel fuel swap, cap, option or similar transaction (or combination thereof) entered into with a Fuel Hedge Counterparty that enables the District to fix or otherwise hedge its budgeted fuel costs, whether for a pre-paid premium or through regularly scheduled payments, based on a published index.

FUEL HEDGE AGREEMENT: A 1992 ISDA Master Agreement, including a Schedule and Credit Support Annex thereto, and a Confirmation reflecting the economic terms of the Fuel Commodity Transactions.

FUEL HEDGE COLLATERAL PROVISION: A provision that requires a Fuel Hedge Counterparty to deliver daily collateral (in the form of U.S. cash or U.S. Treasury obligations) if such counterparty's (or its guarantor's) long-term debt rating becomes rated below "A3" or "A-" by one or more nationally recognized statistical rating organization.

FUEL HEDGE TERMINATION PROVISION: A provision that permits the District to early terminate the Fuel Commodity Transaction if the Fuel Hedge Counterparty's (or its guarantor's) long-term debt rating becomes rated below "Baa2" or "BBB" by one or more nationally recognized statistical rating organization.

FUEL HEDGE COUNTERPARTY: A financial institution or recognized commodity hedge counterparty which, at the time of execution of a Fuel Commodity Transaction with the District, has (or is guaranteed by a party that has) a long-term debt rating (i) in at least the "Aa" or "AA" category by at least one nationally recognized statistical rating organization and (ii) no less than "A2" or "A" by any nationally recognized statistical rating organization(s).

GOVERNMENT SECURITIES: An obligation of the U.S. Government, backed by the full faith and credit of the government. These securities are regarded as the highest quality of investment securities available in the U.S. securities market.

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 bid and asked prices is narrow and reasonable size can be done at those quotes.

LOCAL AGENCY INVESTMENT FUND: A voluntary investment fund open to government entities in California that is managed by the State Treasurer's office.

MARKET VALUE: The price at which a security is trading and could presumable be purchased or sold.

MARK-TO-MARKET: The process whereby the book value or collateral value of a security is adjusted to reflect its current fair value.

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

MAXIMUM PERCENTAGE: Eighty percent (80%) of the District's budgeted diesel fuel costs for a fiscal year.

MAXIMUM TERM: With respect to each Fuel Commodity Transaction, no more than eighteen months.

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

NATIONAL ASSOCIATION OF SECURITIES DEALERS (NASD): A self-regulatory organization (SRO) of brokers and dealers in the over-the counter securities business. Its regulatory mandate includes authority over firms that distribute mutual fund shares as well as other securities.

NOTE: A written promise to pay a specified amount to a certain entity on demand or on a specified date.

OFFER: An indicated price at which market participants are willing to sell a security or commodity. Also referred to as the "Ask Price."

PAR VALUE: The amount of principal which must be paid at maturity. Also referred to as the face amount of a bond, normally quoted in $1,000 increments per bond.

PORTFOLIO: Collection of securities held by an investor.

PRINCIPAL: The face value or par value of a debt instrument, or the amount of capital invested in a given security.

PRUDENT PERSON RULE: An investment standard. California Government Code requires that a fiduciary may invest money only in a list of securities selected by the state-the so-called legal list. In addition, the fiduciary can only invest in a security if it is one which would be bought by a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital.

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.

QUALIFIED PUBLIC DEPOSITORIES: A financial institution which does not claim exemption from the payment of any sales or compensating use or ad valorem taxes under the laws of this state, which has segregated for the benefit of the commission eligible collateral having a value of not less than its maximum liability and which has been approved by the Public Deposit Protection Commission to hold public deposits.

RATE OF RETURN: The yield obtainable on a security based on its purchase price or its current market price. This may be the amortized yield to maturity on a bond or the current income return.

REPURCHASE AGREEMENT (REPO): The purchase of securities by a local agency pursuant to an agreement by which the counterparty will repurchase the securities on or before a specified date and for a specified amount and the counterparty will deliver the underlying securities to the local agency by book entry, physical delivery, or by third party custodial agreement. Refer to section 10.0 for detailed information on the District's collateralization policy.

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.

SECONDARY MARKET: A market made for the purchase and sale of outstanding issues following the initial distribution.

SECURITIES & EXCHANGE COMMISSION (SEC): Agency created by Congress to protect investors in securities transactions by administering securities legislation.

TREASURY BILLS: 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 securities having initial maturities of more than ten years.

TREASURY NOTES: Intermediate term coupon bearing U.S. Treasury securities having initial maturities of from one to ten years.

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 period from the date of purchase to the date of maturity of the bond.