

CAYUCOS SANITARY DISTRICT

INVESTMENT POLICY (Revised October 17, 2013)

I. Scope

This investment policy applies to all financial assets and unrestricted cash reserves of the Cayucos Sanitary District including money market checking account, money market investment accounts, Local Agency Investment Fund (LAIF) pooled money investment account established and administered by the state, and brokerage investment accounts.

II. General Objectives

The primary objective, in priority order, of investment activities shall be safety, liquidity, and yield:

1. Safety. Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to attempt to mitigate credit risk and interest rate risk.

a. Credit Risk. The District will attempt to minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

Limiting investments to the safest types of securities

Pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisers with which the District will do business

Diversifying the investment portfolio so that potential losses on individual securities will be minimized.

b. Interest Rate Risk. The District will attempt to minimize the risk that the market value of securities in the portfolio will fall due to changes in general 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

Investing Operating funds primarily in shorter-term securities, money market mutual funds, or similar investment pools.

2. Liquidity. The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by structuring the portfolio so that securities mature concurrent with cash needs to meet anticipated demands (static liquidity). Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets (dynamic liquidity). A portion of the portfolio also may be

placed in money market mutual funds or local government investment pools which offer same-day liquidity for short-term funds.

3. Yield. The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core of investments are limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed. Securities shall not be sold prior to maturity with the following exceptions:

A security with declining credit may be sold early to minimize loss of principal.

A security swap that would improve the quality, yield, or target duration in the portfolio.

Liquidity needs of the portfolio require that the security be sold.

III. Standards of Care

1. Prudence. The standard of prudence to be used by investment officials (the terms “investment officials”, “Investment Officers” and investment team are used interchangeably throughout this document to refer to those persons responsible for the implementation, management and oversight of the Cayucos Sanitary District’s investment portfolio) 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 may 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 the liquidity and the sale of securities are carried out in accordance with the terms of this policy.

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, and considering primarily the probable safety of their capital as well as the probable income to be derived.

2. Ethics and Conflicts of Interest. Directors, officers and employees involved in the investment process shall refrain from personal business 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 provide written disclosure of any material interests in financial institutions with which they conduct business. They shall further disclose any personal financial/investment positions that could be related to the performance of the investment portfolio. Directors, employees and officers shall refrain from undertaking personal investment transactions with the same individual with whom business is conducted on behalf of the District.

For purposes of this Paragraph 2, a material interest subject to disclosure by Directors, Employees and officers shall include both individual/personal financial interest in a financial institution, and any immediate family members’ (wife, children, parent) financial interest in a financial institution.

3. Delegation of Authority. Authority to manage the investment program is derived from California Government Code Sections 53600, et seq. Management responsibility for the

investment program is hereby delegated to the District Manager, as Investment Officer who shall act in accordance with established written procedures and internal controls for the operation of the investment program consistent with this investment policy. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures, and as provided for in Exhibit A. The Investment Officer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

IV. Safekeeping and Custody

1. Representatives of Authorized Financial Dealers and Institutions. All financial institutions and broker/dealers, their representatives, Registered Investment Advisors and their representatives who desire to become qualified for investment transactions must supply the following as appropriate:

Audited financial statements

Evidence of Financial Industry Regulatory Authority (FINRA) membership and verification of Securities Investment Protection (SIPC) membership

Proof of Broker-Dealer affiliation and/or State or SEC Investment Advisor Registration (Form ADV)

Certification of having read and understood and agreeing to comply with the District's investment policy.

An annual review of the financial condition and registration of qualified financial institutions and broker/dealers will be conducted by the Investment Officer.

2. Internal Controls. The Investment Officer is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the District are protected from loss, theft or misuse. The internal control structure shall be designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived and (2) the valuation of costs and benefits requires estimates and judgments by management.

Accordingly, the Investment Officer shall establish a process for an annual independent review by an external auditor to assure compliance with policies and procedures.

3. Delivery vs. Payment. All trades where applicable will be executed electronically and/or by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible financial institution prior to the release of funds. Securities will be held by a third-party custodian as evidenced by safekeeping receipts.

V. Suitable and Authorized Investments

The Cayucos Sanitary District is empowered by California Government Code Section 53601 et. seq. to deposit and make investment of public funds. For a detailed summary of authorized investment securities, including limitations and special conditions that apply to each, refer to California Government Code Section 53601 et. seq. which is attached and incorporated by reference to this investment policy (Exhibit B).

VI. Investment Parameters

1. Diversification. The investments shall be diversified by:

Limiting investments to avoid over concentration in securities from a specific issuer or business sector (excluding US. Treasury securities),

Limiting investment in securities that have higher credit risks,

Investing in securities with varying maturities, and

Continuously investing a portion of the portfolio in readily available funds such as local government investment pools (LGIPs), LAIF, money market funds or overnight repurchase agreements to ensure that appropriate liquidity is maintained in order to meet ongoing obligations.

It has been the past policy and practice of the District to maintain investments and securities according to the guidelines for specific asset categories as set forth in the California Government Code unless there was a specific and special situation which warranted consideration. At all times, it has been the District's policy to weigh all risks and rewards vs. the District's prudent needs and the Government's guidelines with the objective of avoiding undue investment risk, exposure and concentration. It is recognized that the Board may at some future date, by a duly adopted resolution, adjust this policy if an outlying opportunity becomes evident and that the Board feels justified in pursuing

2. Maximum Maturities. To the extent possible, the District shall attempt to match its investments with anticipated cash flow requirements. While the California Government Code Section 53601 does not specify a limitation on the term or remaining maturity at the time of the investment, no investment shall be made in any security, other than a security underlying a repurchase or reverse repurchase agreement or securities lending agreement authorized by this section, that at the time of the investment has a term remaining to maturity in excess of five years, 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.

Reserve funds and other funds with longer-terms investment horizons may be invested in securities exceeding five (5) years if the maturity of such investments are made to coincide as nearly as practicable with the expected use of funds.

Because of inherent difficulties in accurately forecasting cash flow requirements, a portion of the portfolio should be continuously invested in readily available funds such as LGIPs, LAIF, money market funds, or overnight repurchase agreements to ensure that appropriate liquidity is maintained to meet ongoing obligations.

VII. Reporting

1. Quarterly Report. The Investment Officer shall file a quarterly report (California Government Code Section 53646(b)(1) with the Board of Directors showing the type of investments, institutions, the issuers, maturity dates, par values and the current market

values of each component of the portfolio, including funds managed for Cayucos Sanitary District by third party contracted managers. As specified in California Government Code Section 53646(e), if all funds are placed in LAIF, FDIC-insured accounts and/or in a county investment pool, or any combination of these, the foregoing report elements may be replaced by copies of the latest statements from such institutions. The report must also include a certification that (1) all investment actions executed since the last report have been made in full compliance with the Investment Policy or the manner in which the investment actions are not in compliance and, (2) the Cayucos Sanitary District will meet its expenditure obligations for the next six months or provide an explanation as to why sufficient money shall, or may, not be available as required by California Government Code Section 53646(b)(2) and (3) respectively. The Investment Officer shall maintain a complete and timely record of all investment transactions.

VIII. Investment Strategy

Strategy refers to the ability to manage financial resources in the most advantageous manner.

1. District Reserve Policy. After formulation of the District's annual (fiscal year) budget, and based on projected cash flow forecast and analysis, a determination will be made of projected unrestricted cash reserves to be earmarked for investment (Exhibit C).

2. Economic Forecasts. Gather economic forecasts periodically from investment brokers and other financial experts to assist in formulation of an investment strategy for the District.

3. Rapport. Maintain a close working relationship amongst the investment team members.

4. Implementing Investment Strategy. Execute investment transactions which conform with the current investment plan and anticipated interest rate trends.

IX. Policy Considerations

1. Exemption. Any investment currently held that does not meet the guidelines of this policy shall be, for its stated duration, exempted from the requirements of this policy. At maturity or liquidation, such monies shall be reinvested only as provided by this policy.

2. Amendments. This policy shall be reviewed on an annual basis. Any changes must be approved by the Investment Officer and any other appropriate authority, as well as the individual(s) charged with maintaining internal controls.

X. List of Attachments:

The following documents, as applicable, are attached to this policy:

Roles and Responsibilities of Investment Team (Exhibit A)

Investments Authorized Under California Government Code Section 53601 (Exhibit B)

Reserve Policy (Exhibit C)