

ADDENDUM E

STATEMENT OF INVESTMENT PROCEDURE

I. PURPOSE

- A. This Statement of Investment Procedure sets forth the investment guidelines for all Palomar Pomerado Health ("PPH") investments purchased after March 1, 1996. The purpose of this procedure is to ensure that PPH's funds are prudently invested according to the Board of Director's Policy (FIN – 11) objectives to preserve capital, provide necessary liquidity and to achieve a market-average rate of return through economic cycles.
- B. PPH may invest any portion of surplus funds of its Treasury that is not required for the immediate needs of PPH ("Investable Funds"), subject to the requirements of the California Government Code and PPH Policy (FIN – 11). If the provisions of the Government Code are or become more restrictive than those contained herein, such provisions shall govern, and are deemed incorporated into this procedure upon taking effect.
- C. Government Code Section 53600 et seq., authorizes local agencies to make investments in specified vehicles with money in a sinking fund of, or surplus money in, its treasury not required for the immediate needs of the agency.
- D. PPH is a "local agency" subject to the provision of Government Code Section 53600 et seq., which require the PPH Board of Directors to annually adopt a statement of its investment policy, and to consider any delegation of authority to make investments on its behalf of the Chief Financial Officer.
- E. The Board of Directors of PPH desires to formally adopt a statement of investment policy (FIN – 11) and to re-delegate to the Chief Financial Officer responsibility for all decisions regarding the sale or purchase of individual investments on behalf of PPH.
- F. The PPH Chief Financial Officer is delegated responsibility for all decisions regarding the sale or purchase of individual investments on behalf of PPH.

II. DEFINITIONS:

- A. ***Safety of Principal.*** Safety of principal is the foremost objective of PPH. The safety and risk associated with an investment refers to the potential loss of principal, interest or a combination of these amounts. Each investment transaction shall seek to ensure that capital losses are avoided, whether from institutional default, broker-dealer default, or erosion of market value of securities. To attain this objective, diversification is required in order that potential losses on individual securities do not exceed the income generated from the remainder of the portfolio.

- B. **Liquidity.** Liquidity is the second most important objective of PPH. Liquidity refers to the ability to "cash in" at any moment in 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 occasionally occurs. The investment portfolio shall remain sufficiently liquid to enable PPH to meet all operating requirements that might be reasonably anticipated.
- C. **Yield.** Yield is the potential dollar earnings an investment can provide; it is sometimes described as the rate of return. Within the limits of safety and liquidity, PPH's portfolio growth shall exceed the rate of inflation in order to preserve capital.

III. TEXT / STANDARDS OF PRACTICE

A. Conflicts Of Interest

1. PPH officers and employees involved in the investment process shall refrain from personal business activity in violation of Government Code Section 1090 and the Political Reform Act (Government Code Section 81000 et seq.).
2. Section 1090 of the Government Code prohibits PPH officials from "making" a contract in which the official is financially interested. Under the Political Reform Act, a PPH official is disqualified from making, participating in making, or using his or her official position to influence the making, of a governmental decision in which it is reasonably foreseeable the decision could materially affect the official's economic interest, in a manner distinguishable from its effect on the public generally.
3. In cases of any questions regarding perceived conflicts of interest, the Chief Financial Officer shall forward inquiries to the Chief Executive Officer who, if necessary, shall consult with General Counsel to resolve the inquiry.
4. The Chief Financial Officer shall ensure that investments are not made in organizations that have a line of business perceived to be in conflict with the interests of public health. The Chief Financial Officer shall report such conflicts to the Chief Executive Officer, who shall affirm or reverse the Chief Financial Officer's determination. The Chief Financial Officer also shall ensure that no investments are made in organizations with which PPH has a business relationship through contracting, purchasing or other arrangements.

B. Delegation Of Authority To Chief Financial Officer; Procedures To Implement Investment Policy

1. **Delegation of authority to Chief Financial Officer:** The PPH Chief Financial Officer is delegated responsibility for all decisions regarding the sale or purchase of individual investments on behalf of PPH. This delegation shall be reviewed annually by the Board through the Finance Committee. Any re-delegation shall be

recorded in the minutes of these meeting. No person may engage in an investment transaction except as provided under the terms of this procedure and any other procedures established by the Chief Financial Officer. The Chief Financial Officer shall be responsible for all actions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

2. General Procedures

- a. **Annual review of investment policy.** On an annual basis, the Chief Financial Officer shall review the PPH investment policy with the Finance Committee. After the Finance Committee recommends the policy for presentation to the Board of Directors, the Chief Financial Officer shall present the policy to the Board at its next regular public meeting.
- b. **Annual review by governing board.** The Board of Directors through the Finance Committee shall annually review the investment policy upon presentation by the Chief Financial Officer, and also shall consider any changes to the policy during the public meeting. The Board shall specifically consider whether to renew the delegation of authority to the Chief Financial Officer to make investments on behalf of PPH.
- c. **Quarterly reports.** The Chief Financial Officer shall render a report of investments not less often than within 30 days of the end of each quarter to the Chief Executive Officer and to the Board of Directors. The report shall conform to the requirements of Government Code Section 53607, and Section 53646(b)-(e) as follows:
 - (1) The report shall address all securities, investments and moneys being invested by or on behalf of PPH.
 - (2) The report shall include:
 - The type of investment.
 - Issuer.
 - Date of maturity, par value and dollar amount invested.
 - If any PPH investments have been placed in the State of California Local Agency Investment Fund ("LAIF"), the San Diego County Investment Pool, FDIC-insured accounts in a bank or savings and loan association, or any combination of these vehicles, the quarterly report may include the most recent statements or reports from those agencies in lieu of the information required above.

- A list of all investment transactions for the quarter, specified by the month in which the transaction occurred. A subsidiary ledger of investments may be used in accordance with accepted accounting practices.
 - The actual average maturity of the entire portfolio, the Chief Financial Officer's average maturity goal, and benchmark indices appropriate for the average maturity goal.
 - A description of any of PPH's funds, investments, or programs that are under the: management of contracted parties, including lending parties. For those funds, investments or programs under the management of any third party that is not also a local agency or LAIF, the report shall also include a current market value as of the date of the report, along with the source of the valuation.
 - A statement that the PPH investment portfolio complies with this policy, or a statement as to the manner in which the portfolio is not in compliance. In the latter case, the report shall detail remedial action to be taken by the Chief Financial Officer to bring the portfolio back into compliance.
 - A statement denoting the ability of PPH to meet its expenditure requirements for the next six months, or an explanation as to why sufficient money shall, or may not be available.
- c. **Monthly review of portfolio.** On a monthly basis, the Chief Financial Officer shall review portfolio performance and shall consider whether the diversification of PPH investments is appropriate, to ensure that risk levels and returns are reasonable and that investments are diversified in accordance with this procedure.
- d. **Financial benchmarks.** PPH's portfolio shall be designed to attain a market-average rate of return through economic cycles given an acceptable level of risk. The performance benchmark for the investment portfolio shall be based upon the market indices for investments of comparable risk and duration. The Chief Financial Officer shall review these performance benchmarks at least annually and shall communicate these benchmarks to the Investment Managers.
- e. **Rating Downgrades.** PPH may from time to time have investments in a security whose rating is downgraded below the quality criteria permitted by this investment policy. The Chief Financial Officer shall be notified by the portfolio manager within two (2) business days of any such security, including any security whose rating is put on notice for possible downgrade, and said security shall be reviewed for action. The Chief Financial Officer shall

Deleted: A

Deleted: immediately

approve the decision to retain the security until maturity, to sell (or put) the security, or put the security on a "watch list" for possible future action.

Deleted: to take other action

- f. **Safekeeping.** Any bonds, notes, bills, debentures, obligations, certificates of indebtedness, warrants, or other evidences of indebtedness in which the funds of PPH are invested shall be held in a custodial account. The Board shall select a suitable custodian(s) to oversee all securities and brokerage transactions. The Custodian(s) shall provide the Chief Financial Officer with a monthly report of all transactions. The Custodian shall be insured for limits not less than 150% of PPH's portfolio value. The custodial account shall be established and maintained pursuant to the terms of a written agreement in compliance with Government Code Section 53608.
- g. **Deposit of funds with county treasury.** The Chief Financial Officer may deposit surplus PPH funds for investment with the San Diego County Treasury only upon the adoption of a resolution by the Board of Directors authorizing such action, and with the consent of the County Treasurer.
- h. **Investment Managers.** PPH authorizes the Chief Financial Officer to hire Investment Managers for the purpose of buying, holding or selling securities in accordance with this procedure. The Chief Financial Officer shall evaluate candidates for the role of Investment Manager(s). Candidates shall be reviewed and approved by the CEO and the Board of Directors. The Chief Financial Officer shall provide all Investment Managers with a copy of this procedure, which shall be appended to the Manager's contract and incorporated by reference. The terms of this procedure shall govern over any inconsistent provision in such contracts. Investment Managers shall certify that they will purchase securities from broker/dealers (other than themselves) or financial institutions in compliance with Government Code Section 53601.5 and this procedure.
 - (1) The Chief Financial Officer shall monitor the performance of the Investment Managers and shall have authority to take appropriate action to replace an Investment Manager for failure to perform within the standards of this procedure or the Government Code.
 - (2) The Chief Financial Officer shall periodically report to the Board of Directors on the performance of the Investment Managers.
 - (3) The Investment Managers shall submit to the Chief Financial Officer timely reports of transaction activities and quarterly performance reports.
 - (4) The Investment Managers shall provide the Chief Financial Officer notice of any significant changes in the ownership, organizational structure, financial condition, or senior management of Investment Manager's firm.

C. General Investment Prohibitions

1. Any investment not specifically authorized by this procedure shall be deemed a prohibited investment.
2. Investment securities shall not be lent to officials responsible for the conduct of PPH investments, including any investment manager or broker.
3. The investment portfolio, or investment portfolios managed by an investment manager, shall not be used as collateral to obtain additional Investable Funds.
4. Investments in derivative securities are not allowed, except as to United States Treasury strips as provided in Section D.2.a. below.
5. Investments in inverse floaters, range notes, or mortgage derived interest-only strips are prohibited.
6. Investments in any security that could result in zero interest accrual if held to maturity are prohibited, except as otherwise permitted by Government Code Section 53601.6.

D. Permitted Investments

1. **Maturity and Term:** All investments in individual securities, unless otherwise specified in this procedure, are subject to a maximum term remaining to maturity of five (5) years. The Board of Directors must grant express written authority, to make an investment or to establish an investment program of a longer term.
 - a. "Maturity" shall mean the stated final maturity date of the security, or the unconditional put option date if the security contains such a provision.
 - b. "Term" shall mean the remaining time to maturity when purchased.
2. **Eligible Instruments and Quality:** PPH manages its Investable Funds in accordance with Government Code Sections 53600 through 53609, under which those making investments on its behalf are deemed to act in a fiduciary capacity. These provisions afford PPH a broad spectrum of investment opportunities so long as the investment is deemed prudent and is allowable under current legislation of the State of California. Investments may be made in the following media subject to the quality restraints below:
 - a. **U.S. Treasuries.** These investments are direct obligations of the United States of America and securities that are fully and unconditionally guaranteed as to the timely payment of principal and interest by the full faith and credit of the United States of America. United States government securities include: Treasury Bills; Treasury Notes and Bonds; and Treasury strips (U.S. Treasury

securities that have' been separated into their component parts of principal and interest payments and recorded as such in the Federal Reserve book-entry record-keeping system).

- b. ***Federal Agency and U.S. Government Sponsored Enterprises Securities.*** These securities represent obligations issued by banks for cooperatives, federal land banks, federal intermediate credit banks, federal home loan banks (FHLB), the Federal Home Loan Bank Board, the Tennessee Valley Authority, or obligations, participations, or other instruments of, or issued by, or fully guaranteed as to principal and interest by, the Federal National Mortgage Association (FNMA); or in guaranteed portions of Small Business Administration notes (SBAs); or in obligations, participation, or other instruments of, or issued by, a federal agency or a United States government-sponsored enterprise. Such federal agencies also include:
- (1) Federal Home Loan Mortgage Corporation (FHLMC).
 - (2) Federal Farm Credit Banks (FFCB).
 - (3) Student Loan Marketing Association (SLMA).
 - (4) Government National Mortgage Association (GNMA).
- c. ***State of California and Local Agency Obligations.*** These investments represent obligations or other debt instruments of, or issued by, the State of California, State agencies or local agencies within the state. Such investments include:
- (1) Registered state warrants, treasury notes or bonds of the State of California, including bonds payable solely out of revenues from a revenue-producing property owned, controlled, or operated by the state, or by a department, board, agency or authority of the state.
 - (2) Bonds, notes, warrants or other evidences of indebtedness of any local agency of the state, including bonds payable solely out of 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.
 - (3) PPH is regarded as a tax-exempt entity, so investments in this category – which are generally “Tax Free” – should be avoided unless taxable or net returns are competitive with alternative approved asset classes.
- d. ***Bankers Acceptances.*** These obligations are bills of exchange or time drafts that a commercial bank "accepts" as its financial responsibility as part of a trade finance process. Such short-term notes are sold at a discount, and are obligations of the drawer (the bank's trade finance client) as well as the bank.

Formatted: Bullets and Numbering

Once accepted, the bank is irrevocably obligated to pay the bankers acceptances upon maturity if the drawer does not.

- (1) No more than 30 percent (30%) of PPH's Investable Funds may be invested in the bankers acceptances of any one commercial bank.
- (2) No more than 40 percent (40%) of PPH's Investable Funds may be invested in all bankers acceptances.
- (3) The maximum term for any bankers acceptances shall be 270 days.

e. **Commercial Paper.** Commercial paper is unsecured promissory notes issued by companies and government entities at a discount. Commercial paper is negotiable, although it is typically held to maturity. To qualify as a permissible PPH investment, commercial paper must conform to all of the following:

- (1) The paper must be of "prime" quality of the highest ranking or of the highest letter and numerical rating as provided by Moody's Investors Service, Inc. or Standard & Poor's Corporation.
- (2) The paper must be issued by corporations that are:
 - Organized and operating within the United States and having total assets in excess of five hundred million dollars (\$500,000,000), and
 - Rated A or better by Moody's or Standard and Poor's for the issuer's debt (other than commercial paper), if any.
- (3) Purchases of eligible commercial paper:
 - Shall not represent more than ten percent (10%) of the outstanding paper of the issuing corporation.
 - Shall not exceed 270 days maturity, as authorized in California State Code Section 53601.
 - Shall not exceed fifteen percent (15%) of PPH's Investable Funds and may not exceed five hundred million dollars (\$500,000,000).
- (4) An additional fifteen percent, or a total of thirty percent, of PPH's Investable Funds may be invested in commercial paper, provided that:
 - The "dollar-weighted average maturity" of the entire amount invested in commercial paper does not exceed 31 days.

Formatted: Indent: Left: 1.5", Hanging: 0.25"
Deleted: 180
Deleted: .

- "Dollar-weighted average maturity" means the sum of the amount of each outstanding commercial paper investment multiplied by the number of days to maturity, divided by the total amount of outstanding commercial paper.
- f. **Negotiable Certificates of Deposit.** These instruments are negotiable (marketable or transferable) receipts for time deposits at a bank or other financial institution for a fixed time and interest rate. The following requirements apply:
- (1) Negotiable certificates of deposit must be issued by a nationally or state-chartered bank or state or federal association (as defined by Section 5102 of the California Financial Code) or by a state-licensed branch of a foreign bank.
 - (2) Certificates of deposit shall have a maximum term of 270 days.
 - (3) No more than thirty percent (30%) of PPH's Investable Funds may be invested in negotiable certificates of deposit.
- g. **Repurchase Agreements.** A repurchase agreement is a purchase of securities by PPH under a simultaneous agreement to sell those securities back at a fixed price on some future date. Investments in repurchase agreements shall strictly conform to Government Code Section 53601(i) and may be made on any investment authorized herein as long as:
- (1) The agreements are subject to the delivery payments of Section.
 - (2) The market value of securities that underlay the agreement shall be valued at one hundred and two percent (102 %) or greater of the funds borrowed against those securities and the value shall be adjusted no less than quarterly.
 - (3) The maximum term for any repurchase agreement shall be one year.
- h. **Reverse repurchase agreements.** A reverse repurchase agreement is a sale of securities by PPH pursuant to an agreement by which PPH will repurchase the securities on or before a specified date. Reverse repurchase agreements are only authorized investments with prior approval of the Board and in strict accordance with Government Code Section 53601(i).
- i. **Medium-Term Maturity Notes.** These securities are notes issued by qualified corporations and depository institutions. Medium-term maturity corporate notes must conform to the following:

- (1) Notes must be rated A or better by two nationally recognized rating services with a maturity of five (5) years or less.
 - (2) Notes must be issued by corporations organized and operating within the United States, or by depository institutions licensed by the federal government or any state, and which operate within the United States.
 - (3) No more than thirty (30%) percent of PPH's Investable Funds shall be invested in medium-term maturity notes.
- j. **Money-Market Mutual Funds.** These are shares of beneficial interest issued by diversified management companies that are money market funds registered with the Securities and Exchange Commission ("SEC") under the Investment Company Act of 1940. The following requirements apply:
- (1) Fund must have attained the highest ranking or the highest letter and numerical rating provided by not less than two nationally recognized statistical rating organizations.
 - (2) Fund must have retained an investment adviser registered or exempt from registration with the SEC with not less than five years of experience managing money market mutual funds with assets under management in excess of five hundred million dollars (\$500,000,000).
 - (3) The purchase price of shares in these mutual funds shall not include any commission that the companies may charge.
 - (4) The combined amount of PPH's Investable Funds invested in both money market funds and other mutual funds shall not exceed forty percent (40%) of the Authority's Investable Funds.
- k. **Other Mutual Funds.** These types of funds consist of shares of beneficial interest issued by diversified management companies that invest in the securities and obligations as authorized below. The following requirements apply:
- (1) Fund must have attained the highest ranking or the highest letter and numerical rating provided by not less than two nationally recognized statistical rating organizations.
 - (2) Fund must have retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience investing in the securities and obligations authorized by Government Code Section 53601(a)-G), or (m) or (n) and with assets under management in excess of five hundred million dollars (\$500,000,000).

- (3) The fund's investments must can farm to these authorized by Government Code Section 53601(a)-G), or (m) or (n).
- (4) The purchase price of shares in these mutual funds shall not include any commission that the companies may charge.
- (5) No more than forty percent (40 %) of the PPH' s Investable Funds shall be invested in bath money market funds and other mutual funds combined.
- (6) No more than 10 percent (10%) of the PPH's Investable Funds may be invested in shares of any one mutual fund.

l. **Pledged Money.** Pledged money is money held by a trustee or fiscal agent and pledged to the payment or security of bonds or other indebtedness or obligations under a lease, installment sale or other agreement of a local agency. PPH may invest in pledged money in accordance with the statutory provisions governing the issuance of those media.

m. **Secured Securities.** A secured security is a note, bond or other obligation that is at all times secured by a valid first priority security interest of the types listed by Government Code Section 53651 as eligible securities for the purpose of securing local agency deposits having a market value at least equal to that required by Section 53652 for the purpose of securing local agency deposits. Secured securities shall be:

- (1) Perfected in accordance with Uniform Commercial Code.
- (2) Placed by delivery or by book entry into the custody of a trust company or the trust department of a bank which is not affiliated with the issues of the secured obligation.

E. DIVERSIFICATION GUIDELINES

- 1. Diversification limits ensure the portfolio is not unduly concentrated in the securities of one type, industry, or entity, thereby assuring adequate portfolio liquidity should one sector or company experience difficulties.
- 2. The following chart summarizes the maximum percentage that each type of permissible investment may constitute within PPH's overall investment portfolio.

<u>Instruments</u>	<u>Maximum % Portfolio</u>
1. United States Treasuries	100%
2. Federal agency and U.S. Government Sponsored Enterprises	100%

Deleted: k

Deleted: *Mortgage or Asset-backed Pass-through Securities.* ¶

¶

<#>Pass-through securities are instruments by which the cash flow from the mortgages, receivables or other assets underlying the security are passed-through as principal and interest payments to the investor. Though these securities may contain a guarantee from the issuer, they are a package of assets being sold, not a debt obligation of the issuer. Other types of "backed" debt instruments have assets (such as leases or consumer receivables) pledged to support the debt service. ¶

¶

<#>Any mortgage pass-through security, collateralized mortgage obligations, mortgage-backed or other pay-through bond, equipment lease-backed certificate, consumer receivable pass-through certificate, or consumer receivable-backed bond is an eligible PPH investment, provided: ¶

¶

<#>The vehicle is rated AA by a nationally recognized rating service. ¶

¶

<#>The issuer has an A or better rating for the issuer's debt as provide by a nationally recognized rating service.¶

¶


<#>The investment vehicle has a maximum stated final maturity of five (5) years. ¶

¶

<#>Purchase of such securities shall not exceed twenty (20%) percent of PPH's Investable Funds. ¶

¶

l. .

3. State of California and Local Agency obligations	25%
4. Bankers acceptances	40%
5. Commercial paper	
If weighted average maturity of all CP is greater than 31 days	15%
If weighted average maturity of all CP is less than 31 days	30%
6. Negotiable Certificates of Deposit	30%
7. Repurchase agreements	100%
Any one repurchase agreement counterparty name	
If maturity/term is <u>< 7 days</u>	50%
If maturity/term is <u>> 7 days</u>	35%
8. Reverse repurchase agreements	20%
9. Medium-term maturity corporate securities	30%
10. Money market funds and other mutual funds (in total)	20%
11. 	
12. Pledged money	100%
13. Secured securities	100%

Deleted: Mortgage and asset-backed securities

Deleted: 20%

F. This procedure and the Board Policy will be reviewed and updated as required or at least every year.

IV. DOCUMENT / PUBLICATION HISTORY:

Original Document Date: 7/14/95
 Reviewed:
 Revision Number: 1 Dated: 6/06
 Document Owner: Michael Covert
 Authorized Promulgating Officers: Marcelo R. Rivera, Chairman

VI. CROSS REFERENCE DOCUMENTS:

- A. Prior to 2006, this was included as part of Board Policy 10-513
- B. Board Policy FIN - 11