

DEPARTMENT OF WATER AND POWER
CITY OF LOS ANGELES

TRUST FUNDS INVESTMENT POLICY

FINANCIAL SERVICES ORGANIZATION
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TRUST FUNDS INVESTMENT POLICY

I. INTRODUCTION

The City Charter grants the Board of Water and Power Commissioners (“Board”) control over the investment of all financial assets of the Department of Water and Power (“Department”). Proposition “T”, approved on November 5, 1996, permits the Department the flexibility to invest its funds in accordance with the California Government Code (“Code”), Section 53600 through 53686.

A majority of the Department’s financial assets are in the Power and Water Revenue Funds. These assets have been part of the City of Los Angeles’ investment pool program since 1983. However, certain financial assets of the Department held in special-purpose trust or escrow funds (“Trust Funds”) with an independent trustee are not included in the City’s investment pool program.

II. PROGRAM SCOPE

The Department’s Trust Funds Investment Policy (“Investment Policy”) applies to all financial assets of the Department other than those held in the Power and Water Revenue Funds. Financial assets held in the Power and Water Revenue Funds are managed by the City Treasurer within the guidelines established by the investment policy of the City of Los Angeles.

This Investment Policy applies to the Trust Funds listed below.

- Electric Plant Revenue Bond Reduction Escrow Fund

This trust fund, commonly referred to as the Debt Reduction Trust Fund (“DRTF”), was established through Board Resolution No. 97-116 approved in November 1996 to serve as depository for funds accumulated for debt restructuring. Debt reduction was necessary to improve the Department’s financial position in response to changes in the power industry’s competitive structure.



- Palo Verde Nuclear Decommissioning Trust Funds I and II

In March 1988, a decommissioning trust account was established through Board Resolution No. 88-193 with the City Treasurer as custodian of funds. In October 1990, the Department converted this account into two external decommissioning trust funds (“Trust Fund I” and “Trust Fund II”) and hired a trustee as custodian due to the Nuclear Regulatory Commission (“NRC”) requirement that decommissioning funds be held in a trust.

Trust Fund I was established to meet the NRC’s funding guidelines, whereas Trust Fund II was established to meet the funding difference between the NRC and the Arizona Nuclear Power Project Participation Agreement’s funding requirements. In addition to the guidelines established by this Investment Policy, both trust funds must adhere to the criteria and standards developed by the Palo Verde Nuclear Generating Station’s Termination Funding Committee.

- Natural Gas Trust Fund

This trust fund was established through Board Resolution 004-021 approved in July 2003, and amended in October 2003, to serve as a depository for funds provided for the purpose of posting margin or collateral, and to pay all fees and expenses incurred in connection with natural gas transactions entered into by the Department.

- Water Expense Stabilization Fund

This trust fund was established in accordance with the Water System Master Bond Resolution No. 4591, approved on February 6, 2001, to be used for any lawful purpose in connection with the Water System including operation and maintenance, debt service, costs of debt issuance, and/or capital improvements.

- Treatment Storage and Disposal Facility (TSDF) Trust Fund

This trust fund was established through Board Resolution 009-037 approved in August 2008, and amended in April 2010, to provide financial assurance for closure of the Main Street TSDF.



- California Independent System Operator (CAISO) Markets Trust Fund

This trust fund was established in accordance with Board Resolution 021-138, approved in February 2021, to facilitate timely and efficient settling of CAISO energy market transaction invoices.

Additionally, this Investment Policy shall apply to special purpose trust or escrow funds established by the Board in the future unless otherwise exempted.

III. STATEMENT OF POLICY

The Investment Policy establishes investment objectives and constraints to manage the investment portfolio and enhance the income from and cash flows of the Trust Funds. Each Trust Fund has a unique purpose, maturity horizon, cash flow pattern, and investment requirements. The general policy, as it relates to investing the Trust Funds, is to preserve the principal value, maintain the liquidity, and maximize income of the Trust Funds. This Investment Policy will be adhered to through consistent, safe, and prudent investment practices, which incorporate recognized portfolio management techniques.

The purpose of this Investment Policy is to establish cash management and investment policy and guidelines for the Department's Chief Financial Officer ("CFO"), who is ultimately responsible for the stewardship of the Trust Funds. Each transaction and the entire portfolio must comply with the California Government Code Section 53600 through Section 53686 and this Investment Policy. All Trust Funds investment activities will be judged by the standards of the Investment Policy and ranking of investment objectives. Any activity that violates its spirit and intent will be deemed to be contrary to the Investment Policy.

IV. INVESTMENT OBJECTIVES

All financial assets should be invested prudently to earn a reasonable return prior to specific application of funds. Investments should be made with precision and care considering the probable safety of the capital as well as probable income to be derived. The Department will administer an



investment program that will ensure the accomplishment of three specific objectives. These objectives are ranked below in order of importance.

1. Safety

The Department's first objective is to preserve the Trust Funds' value by establishing a system of controls that is adequate to protect against fraud or mismanagement and by instituting prudent practices to manage portfolio risk. Examples of prudent practices to manage portfolio risk include establishing a target average duration or maturity, a minimum rating standard for corporate investments, and appropriate diversification standards to control market risks.

The CFO's goal is to safeguard the principal of funds invested. However, the CFO may elect to sell a security prior to its maturity and record a capital gain or loss to improve the quality, liquidity, or yield of the portfolio in response to market conditions or change in risk preferences.

2. Liquidity

The Department's second objective is to ensure that investments are consistent with each individual Trust Fund's cash needs, and allow rapid conversion to cash without substantial loss in value. Liquidity may be achieved by matching the investment horizon of financial assets with the cash flow requirements of the Trust Funds and purchasing investments that are readily marketable.

3. Yield/Return

The Department's third objective is to achieve the maximum yield/return without compromising the safety and liquidity of principal. The Trust Funds' performance will be compared to the performance of market indices of similar duration and sector allocation, for benchmarking purposes.



V. DELEGATION OF AUTHORITY

The overall responsibility for managing the investment program is delegated to the Auditor, the CFO, by definition of the duties and responsibilities of the position. The CFO directs the 'Trust Funds' investment activities through the Department's Assistant CFO and Treasurer or his/her designee.

No person may engage in an investment transaction except as provided under the terms of this Investment Policy and the procedures established by the Assistant CFO and Treasurer or his/her designee. Only persons authorized by the Board can invest the monies of the Trust Funds.

The Assistant CFO and Treasurer or his/her designee shall establish written procedures for the operation of the investment program including all investment transactions consistent with this Investment Policy. These written procedures, as well as all investment strategies, are subject to approval by the Investment Committee.

VI. INVESTMENT COMMITTEE

An Investment Committee ("Committee") has been established pursuant to Board Resolution No. 97-185 approved in March 1997. The Committee currently consists of the City Controller or his/her designee, a Board Member designated by the Board President, the General Manager of the Department or his/her designee, and the Chief Financial Officer.

The Committee shall meet on an as needed basis, but at least annually to approve revisions to the Investment Policy, to determine/discuss general investment strategies, and to monitor investment results.

The Committee meetings may include discussions about topics such as: 1) the overall economic outlook for the 'Trust Funds, 2) the diversification and maturity structure of the current investment portfolio, 3) potential risks to the 'Trust Funds, 4) current status of all authorized brokers and dealers, 5) the yield/return achieved on the 'Trust Funds, and 6) future investment strategy.



The Committee shall establish its own rules of procedures, and shall perform such other duties as may be assigned to it by this Investment Policy or upon motion by the Board.

Decisions and recommendations made by the Committee shall be based on achieving a consensus among members of the Committee. In the absence of a consensus, the item(s) may be submitted to the Board for consideration at the discretion of the Chair of the Committee.

VII. STANDARD OF CARE

Investment personnel shall use the “Prudent Investor” standard when investing monies in the Trust Funds. This standard shall be applied in the context of managing all aspects of the Trust Funds.

The California Government Code Section 53600.3 states that

“... all governing bodies of local agencies or persons authorized to make investment decisions on behalf of those local agencies investing public funds pursuant to this chapter are trustees and therefore fiduciaries subject to 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. Within the limitations of this section and considering individual investments as part of an overall strategy, investments may be acquired as authorized by law.”

VIII. INTERNAL CONTROL

The Assistant CFO and Treasurer or his/her designee shall establish a system of internal controls to provide reasonable assurance that the Trust Funds’ investment objectives are met and to ensure that the Trust Funds’ assets are protected from fraud, loss, theft, and misuse. The Assistant CFO and Treasurer or his/her designee shall also be responsible for ensuring that all investment transactions comply with the Investment Policy.



IX. INVESTMENT OF FUNDS

A. AUTHORIZED INVESTMENTS

Investment of the Department's Trust Funds is governed by the Code Sections 53600 through 53686.

Authorized investments shall also include investments into the Local Agency Investment Fund ("LAIF") in accordance with Code Section 16429.1, or the Los Angeles County Pool Fund in accordance with Code Section 53684. Below are the investment instruments authorized for the Trust Funds. In the event of a discrepancy between this Investment Policy and the Code, the more restrictive parameters shall take precedence.

Compliance with the percentage limitations established in this Investment Policy will be evaluated on a combined basis across all funds invested under this Investment Policy. Percentage limitations on the purchase of securities apply at the time of purchase. Credit ratings, where shown, specify the minimum credit rating category required at purchase without regard to modifiers (+/- or 1, 2, 3), if any. For split rated securities, the security's or issuer's highest applicable rating issued by a nationally recognized statistical rating organization ("NRSRO") will be used for determining the security's compliance with this Investment Policy.

1. U. S. GOVERNMENT SECURITIES such as U.S. Treasury notes, bonds, bills, or certificates of indebtedness, or those for which the faith and credit of the United States are pledged for payment of principal and interest. There is no percentage limitation of the portfolio that can be invested in this category, although a five-year maturity limitation is applicable except for investments in the Palo Verde Nuclear Decommissioning Trust Funds, which may be extended to 30 years.

2. FEDERAL AGENCY AND UNITED STATES GOVERNMENT SPONSORED ENTERPRISE OBLIGATIONS including participations or other instruments guaranteed as to principal and interest by federal agencies, such as the Government National Mortgage Association ("GNMA"), the Tennessee Valley Authority ("TVA"), and the Small



Business Administration ("SBA"); or U.S. government-sponsored enterprises, such as the Federal Farm Credit Bank ("FFCB"), the Federal Home Loan Bank ("FHLB"), the Federal National Mortgage Association ("FNMA"), the Federal Home Loan Mortgage Association ("FHLMC"),. There is no percentage limitation of the portfolio that can be invested in this category except that a maximum of 30% of the cost value of the portfolio may be invested in any one Agency issuer name. A five-year maturity limitation is applicable except for investments in the Palo Verde Nuclear Decommissioning Trust Funds, which may be extended to 30 years.

The types of securities offered by Federal Agencies or Government Sponsored Enterprises that may be purchased include, but are not limited to, fixed rate bonds, step rate bonds, variable rate bonds, conversion bonds, and discount notes.

Investments detailed in items no. 3 through 16 (except item nos. 9, 10, 13, and 15) are further restricted to percentage of the cost value of the portfolio in any one issuer name or placed through a deposit placement service to a maximum of 10%. The total value invested in any one issuer shall not exceed 5% of the issuer's net worth. Again, a five-year maximum maturity limitation is applicable unless further restricted by this investment policy.

3. SUPRANATIONALS 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. Investments shall be rated "AA" or better, or the equivalent, by a NRSRO. Purchases of supranationals may not exceed 30% of the cost value of the portfolio. A maximum of 10% of the portfolio may be invested in any one issuer name.

4. BANKERS ACCEPTANCES also known as bills of exchange or time drafts drawn on and accepted by commercial banks of "prime" quality of the highest ranking or of the highest letter and number rating (i.e., A-1, P-1, F-1, etc.) as provided for by at least two NRSROs. Purchases



of bankers acceptances may not exceed 180 days to maturity or 40% of the cost value of the portfolio. A maximum of 10% of the portfolio may be invested in any one issuer name. For Yankee Bankers Acceptances, only those of the highest credit rating (i.e., A-1+, P-1, F-1+, etc.) by at least two NRSROs may be purchased.

5. COMMERCIAL PAPER of “prime” quality of the highest ranking or of the highest letter and number rating as provided for by at least two NRSROs. To be eligible for purchase, the entity that issues the commercial paper shall meet all of the following conditions in either paragraph (a) or paragraph (b) below:

- i. The entity must meet the following criteria:
 1. Is organized and operating in the United States as a general corporation.
 2. Has total assets in excess of \$500,000,000.
 3. Has debt other than commercial paper, if any, that is rated “A” or higher, or the equivalent, by a NRSRO.
- ii. The entity must meet the following criteria:
 1. Is organized within the United States as a special purpose corporation, trust, or limited liability company.
 2. Has program-wide credit enhancements including, but not limited to, overcollateralization, letters of credit, or surety bond.
 3. Has commercial paper that is rated “A-1” or higher, or the equivalent, by at least two NRSROs.

Purchases of eligible commercial paper may not exceed 270 days to maturity. Purchases of commercial paper may not exceed 40% of the cost value of the portfolio. A maximum of 10% of the portfolio may be invested in any one issuer name.

In addition to the above requirements, the following criteria are applicable for purchases of asset-backed commercial paper:

- Program size of at least \$5 billion.
- Minimum of at least two broker/dealers supporting the deal.
- Seasoned deal – more than 1 year outstanding in the marketplace.



- Sponsor bank short-term rating of the highest letter and number as provided for by at least two NRSROs.
- For fully supported programs, there must be one or more liquidity providers, each rated “A-1” or higher, or the equivalent, by at least two NRSROs, whose aggregate commitment to ensure payment equals at least the total principal outstanding and accrued interest at any time.
- For partially supported programs, at least 95% of the securities in the issuer’s portfolio must be investment grade, program credit ratings must be affirmed by the NRSROs prior to inclusion of any non-securities assets (mortgages, receivables, etc.) in the portfolio, and program-wide credit support must be provided by either cash collateral or a third party that has a short-term rating of at least “A-1” or higher, or the equivalent, by at least two NRSROs.

A list of commercial paper issuers that meet the Department’s criteria has been established. The list is dynamic and issuers may be added or removed periodically.

6. NEGOTIABLE CERTIFICATES OF DEPOSIT issued by nationally or state-chartered banks, state or federal savings associations, a state or federal credit union or a federally-licensed or state-licensed branch of foreign bank (Yankee CDs) of “prime” quality of the highest ranking or of the highest letter and number rating as provided for by at least two NRSROs. Purchases of negotiable certificates of deposit may not exceed 30% of the cost value of the portfolio. A maximum of 10% of the portfolio may be invested in any one issuer name. A maturity limitation of 397 days is applicable.

7. PLACEMENT SERVICE DEPOSITS placed through a deposit placement service that meet the requirements of Code Section 53601.8. The full amount of the principal and interest that may be accrued during the maximum term of any deposit shall be 397 days. Purchases of Placement Service Deposits may not exceed 30 percent of the cost value of the portfolio. A maximum of 10% of the portfolio may be invested through any one private sector entity that assists with the placement of deposits.



8. REPURCHASE AGREEMENTS that specify terms and conditions may be transacted with banks and broker dealers. The maturity of the repurchase agreements shall not exceed 92 days. The market value of the securities used as collateral for the repurchase agreements shall be monitored by the trustee bank/custodian and shall not be allowed to fall below 102% of the value of the repurchase agreement. A Public Securities Association ("PSA") Master Repurchase Agreement is required between the Department and the broker dealer or financial institution for all repurchase agreements transacted. A maximum of 10% of the portfolio may be invested in any one issuer name.

9. REVERSE REPURCHASE AGREEMENTS that specify terms and conditions may be transacted with broker dealers and financial institutions, but the total of all reverse repurchase agreements and securities lending agreements on investments owned by the Department cannot exceed 20% of the cost value of the portfolio on the date on which any of these agreements is entered into. The security to be sold on reverse purchase agreements must have been owned at least 30 days prior the sale. The Department may enter into reverse repurchase agreements only to fund short-term liquidity needs. The term of reverse repurchase agreements may not exceed 92 days.

10. CALIFORNIA LOCAL AGENCY INVESTMENT FUND ("LAIF") is a State of California managed investment pool, which may be used up to the maximum permitted by California State law.

11. MORTGAGE-BACKED AND ASSET-BACKED OBLIGATIONS rated in a rating category of "AA" or its equivalent or better by a NRSRO. Purchases of these securities may not exceed 20% of the cost value of the portfolio and are limited to a maturity of no longer than 5 years. A maximum of 10% of the portfolio may be invested in any one issuer name.

12. MEDIUM-TERM CORPORATE NOTES issued by corporations organized and operating within the U.S. or by depository institutions licensed by the U.S. or any state and operating within the U.S. with a maximum remaining maturity of five years may be purchased. Securities eligible for investment shall be rated in a rating category of "A" or its equivalent or better by a NRSRO. Purchases of medium-



term notes may not exceed 30% of the cost value of the portfolio. A maximum of 10% of the portfolio may be invested in any one issuer name.

13. MONEY MARKET FUNDS may be purchased as allowed under State of California Government Code. Purchases of eligible money market funds may not exceed 20% of the cost value of the portfolio.

14. STATE OF CALIFORNIA OBLIGATIONS such as warrants, treasury notes, or bonds, including bonds payable solely out of the revenues from a revenue producing property owned, controlled, or operated by the State or by a department, board, agency, or authority of the State with a maximum remaining maturity of five years may be purchased. Securities eligible for investment shall be rated in a rating category of "A" or its equivalent or better by a NRSRO at the time of purchase. There is no percentage limitation of the portfolio that can be invested in this category except that a maximum of 10% of the cost value of the portfolio may be invested in any one issuer of the State, department, board, agency, or authority of the State.

15. CALIFORNIA LOCAL AGENCY OBLIGATIONS such as notes, warrants, or bonds, 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 with a maximum remaining maturity of five years may be purchased. Securities eligible for investment shall be rated in a rating category of "A" or its equivalent or better by a NRSRO at the time of purchase. Authorized investments in this category include securities issued by the Department's Water System and Power System and Southern California Public Power Authority. There is no percentage limitation of the portfolio that can be invested in this category. Investments in securities issued by the Department's Water System and Power System and Southern California Public Power Authority, combined are restricted to a maximum of 20% of the cost value of the portfolio. For all other California local agency obligations, a maximum of 10% of the cost value of the portfolio may be invested in any one issuer.



16. STATE (OTHER THAN CALIFORNIA) OBLIGATIONS such as notes or bonds of any of the other 49 states in addition to California, 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 any of the other 49 states, in addition to California, with a maximum remaining maturity of five years may be purchased. Securities eligible for investment shall be rated in a rating category of “A” or its equivalent or better by a NRSRO at the time of purchase. There is no percentage limitation of the portfolio that can be invested in this category except that a maximum of 10% of the cost value of the portfolio may be invested in obligations issued by any one state.

The following table summarizes investment parameters, by instrument, that have been established for the Department’s Trust Funds.



*DEPARTMENT OF WATER AND POWER
CITY OF LOS ANGELES*

	<i>Instrument</i>	<i>Maximum Maturity</i>	<i>Maximum Concentration</i>	
			<i>By Category</i>	<i>By Issuer</i>
1	U.S. Government Securities	5 years; 30 years for Decommissioning Trust Fund	100%	100%
2	Federal Agency and U.S. Government Sponsored Enterprise Obligations	5 years; 30 years for Decommissioning Trust Fund	100%	30%
3	Supranationals	5 years	30%	10%
4	Bankers Acceptances	180 days	40%	10%
5	Commercial Paper	270 days	40%	10%
6	Negotiable Certificates of Deposit	397 days	30%	10%
7	Placement Service Deposits	397 days	30%	10%
8	Repurchase Agreements	92 days	100%	10%
9	Reverse Repurchase Agreements	92 days	20%	N/A
10	California Local Agency Investment Fund	N/A	100%	100%
11	Mortgage-Backed and Asset-Backed Obligations	5 years	20%	10%
12	Medium Term Corporate Notes	5 years	30%	10%
13	Money Market Funds	N/A	20%	20%
14	State of California Obligations	5 years	100%	10%
15	CA Local Agency Obligations	5 years	100%	10%*
16	State (Other than CA) Obligations	5 years	100%	10%

**For California local agency obligations a maximum of 10% may be invested in any one issuer, except for obligations of LADWP and Southern California Public Power Authority, in which a combined maximum of 20% may be invested.*

B. MAXIMUM MATURITIES

Unless specified in the Code, the maximum maturity for permissible investments is five years. However, investments may be purchased with a remaining maturity of greater than five years provided the legislative body grants express authority to make the investment either specifically or as part of an investment program approved by the legislative body at



least three months prior to purchase. The Board passed Board Resolution No. 000-108 on December 7, 1999, increasing the maximum maturity for U.S. Government Securities and Federal Agency and U.S. Government Sponsored Enterprise Obligations from five to 30 years for the Palo Verde Nuclear Decommissioning Trust Funds I and II.

An investment's term or remaining maturity shall be measured from the settlement date to final maturity. Unless otherwise allowed under the Code, a security purchased shall not have a forward settlement date exceeding 45 days from the time of investment.

For investment instruments with a tender or put option for the holder to tender such investment for purchase at the par amount thereof plus accrued and unpaid interest, the maturity of such investment for purposes of this Investment Policy shall be deemed to be the period between the date of purchase and the first time thereafter such tender or put option can be exercised.

C. PROHIBITED INVESTMENTS

No investment shall be authorized that has the possibility of returning a zero or negative yield if held to maturity, except as allowed for U.S. Government Securities pursuant to Section 53601.6 of the Code, in the event of, and for the duration of, a period of negative market interest rates.

Prohibited investments include, but are not limited to, inverse floaters, range notes, or interest-only strips derived from a pool of mortgages.

D. EQUITY-LINKED NOTES

An equity-linked note is a debt obligation of a corporate issuer that provides the investor a return tied to the performance of a particular stock index or basket of stocks. Unlike typical bond offerings, it pays little or no semiannual coupon. At maturity, it repays all or a portion of the principal plus a return that is based on the performance of the chosen index. This return is referred to as the supplemental redemption



amount. The supplemental redemption amount may be zero, but will not be less than zero.

In October 1999, the Board passed Resolution No. 000-080 authorizing the purchase of Equity Linked Notes in the Palo Verde Nuclear Decommissioning Trust Funds and the Postretirement Healthcare Benefit Trust Fund. At a minimum, a guaranteed return of one percent shall be required for an equity-linked note. The equity participation rate shall be adjusted to achieve this minimum requirement.

Equity-linked notes shall be categorized as medium-term corporate notes as defined under the California Government Code. They shall be limited by the same constraints applicable to corporate notes under the Code and Section IX.A (Authorized Investments) of this Investment Policy, except that purchases of equity-linked notes shall not exceed 5 percent of the cost value of the portfolio. Investment in equity-linked notes is further restricted to the percentage of the cost value of the portfolio in any one issuer name to a maximum of 5 percent. The total value invested in any one issuer shall not exceed 5 percent of the issuer's net worth. A five-year maximum maturity limitation is applicable.

E. INTEREST EARNINGS

All moneys earned and collected from investments authorized in this Investment Policy shall remain in the individual Trust Funds or accounts.

F. PORTFOLIO MANAGEMENT ACTIVITY

The investment program shall seek to augment returns consistent with the intent of this Investment Policy, identified risk limitations, and prudent investment principles. These objectives may be achieved through the use of any strategies listed below.

Active Portfolio Management. The portfolio yield may be enhanced with limited and calculated increases in risk through active fund and



cash flow management taking advantage of current economic and interest rate trends.

Portfolio Maturity Management. Investment personnel shall evaluate current and expected interest rate yields and necessary cash flow requirements when structuring the maturity composition of the portfolio. It is recognized that, in normal market conditions, longer maturities produce higher yields. However, securities with longer maturities also experience greater price fluctuations when interest rate levels change.

Security Swaps. A security swap involves switching one security for another and is entered into for a variety of reasons. Swaps are executed to increase portfolio yield, to lengthen or shorten maturities or duration, to take a profit, or to improve investment quality.

The Department may take advantage of security swap opportunities to improve the overall portfolio yield. A swap that improves the portfolio yield may be selected even if the transaction results in an accounting loss. Documentation of swaps will be included in the Department's permanent investment file documents. Under no circumstances shall a swap be used solely for purposes of speculation.

Competitive Bidding. Competitive bidding is required for all investment transactions except for new issue securities, securities bought directly from the issuer, and liquidation to reduce future losses on securities of companies with financial difficulties that are or are expected to experience rapidly declining market value. When competitive bidding is required, at least three bidders must be contacted for the purchase and sale of any security. When competitive bidding is not required, the price of the trade should be compared to an independent financial source to verify current market pricing, and such pricing must be documented for auditing purposes.

G. COLLATERAL REQUIREMENTS

Security collateral is required for investments in repurchase agreements. Repurchase agreements executed with approved brokers or dealers



must be collateralized with either U.S. Government Securities, or Federal Agency and U.S. Government Sponsored Enterprise obligations.

In order to reduce market risk, the market value of the collateral (principal and accrued interest) shall be at least 102 percent of the repurchase agreement. Since the market value of the underlying securities is subject to daily market fluctuations, investments in repurchase agreements shall be in compliance if the value of the underlying securities is brought back up to 102 percent no later than the next business day. Use of mortgage-backed securities for collateral is not permitted except for securities lending transactions.

H. LIMIT MARKET VALUE EROSION

The longer the maturity of securities, the greater the market price volatility. Therefore, it is the general policy of the Department to limit the potential effects from erosion in market values by adhering to the guidelines below.

- All immediate and anticipated liquidity requirements will be addressed before purchasing any investments.
- Maturity dates for investments will coincide with significant cash flow requirements where possible.
- All long-term securities will be purchased with the intent to hold investments to maturity under then prevailing economic conditions. However, economic market conditions may change, making it in the Department's best interest to sell or trade a security prior to maturity.

I. DIVERSIFICATION

Assets in the Trust Funds shall be diversified to minimize the risk of loss resulting from an over-concentration of assets in a specific maturity, industry, issuer, or sector.



J. SAFEKEEPING

All securities purchased shall be delivered against payment and held in safekeeping pursuant to a safekeeping agreement with a third party custodian/trustee. The custodian/trustee shall be required to provide safekeeping receipts and ongoing reports to verify securities taken into possession. The only exceptions to the foregoing shall be collateralized and/or insured time deposits, LAIF, and money market mutual funds since these securities are not deliverable. Evidence of each of these investments shall be maintained by the custodian/trustee.

Securities held in custody for the Department shall be independently audited on an annual basis to verify investment holdings. Any exceptions to this safekeeping policy must be approved by the CFO in writing and included in reports to the Board and the Investment Committee.

K. RISKS

The Department recognizes that investment risks can result from issuer defaults, market price changes, or various technical complications leading to temporary illiquidity. Portfolio diversification is employed as a means to control risks in addition to establishing prudent selection of securities by investment personnel.

No individual investment transaction shall be undertaken which jeopardizes the total capital position of the overall portfolio. In the event of default by a specific issuer, the CFO will take immediate action and evaluate the security for possible liquidation.

X. AUTHORIZED BROKERS/DEALERS

The Assistant CFO and Treasurer or his/her designee shall maintain a list of broker/dealers authorized to provide investment services to the Department. An authorized broker or dealer must acknowledge in writing to the Assistant CFO and Treasurer or his/her designee that the broker has received and read a copy of this Investment Policy before conducting trades on behalf of the Department. All brokers or dealers will be selected based upon an evaluation of their credentials by the Assistant CFO and Treasurer.



or his/her designee as outlined in Appendix B. Investment personnel shall conduct trades on behalf of the Department only with authorized investment brokers or dealers.

XI. SECURITIES LENDING PROGRAM

The CFO is authorized to engage contractors to perform securities lending activities or allow custodian banks to subcontract for securities lending services. The securities lending program is governed by a separate policy and procedures/guidelines as shown in Appendix A of this Investment Policy.

XII. PROFESSIONAL SERVICES

The Department may contract for outside professional services, such as a master custodian, securities lending agent, and investment advisor, as necessary for the efficient and prudent management of investments.

At least annually, the Department shall contract for the services of an independent third party or require the Department's external auditor to review the investment operations, including policies, procedures, and controls, and to submit the results of the review to the Committee.

XIII. REPORTING

The Assistant CFO and Treasurer or his/her designee shall submit quarterly investment reports that summarize investment income to the Committee and the Board for information and evaluation.

Pursuant to California Government Code section 53646, the report will list the type of investments, name of issuer, maturity date, par and dollar amount of the investments. For the total investment program, the report will list average maturity, market value, and pricing source of the investments. The report shall also show portfolio yields/returns, portfolio risks (modified duration and weighted average life), benchmark yields/returns, and portfolio allocation by investment instrument, term, and credit ratings. Additionally, the report will include a description of any funds under the management of contracting parties (including securities lending programs), a statement of compliance to the Investment Policy, and a



statement of the Trust Funds' ability to meet the expected expenditure requirements for the next six months.

Exceptions to the Investment Policy shall be reported as established in the Exceptions Handling and Reporting section of the attached Investment Guidelines.

XIV. POLICY REVIEW

The Investment Policy shall be adopted through a Board resolution annually. The Investment Policy shall be reviewed at least once a year to ensure its consistency with the overall objectives of safety, liquidity, and yield/return, as well as its relevance to current law and financial and economic trends. Any amendments to the Investment Policy shall be forwarded to the Board for approval.

Any changes or amendments to the Code resulting from legislative action by the State of California shall be deemed incorporated in the Investment Policy and shall supersede any and all previous applicable language. The Investment Policy will be revised to reflect such changes or amendments during its next submittal to the Board for approval.



XV. TRUST FUNDS INVESTMENT GUIDELINES

1. AUTHORIZATIONS AND RECORDS RETENTION

- a. All brokers and/or dealers with whom investment personnel deal must be approved by the Assistant CFO and Treasurer or his/her designee prior to any transaction.
- b. Investment personnel shall maintain a current listing of all institutions approved as authorized brokers and/or dealers.
- c. Subject to Section IX.F of this Investment Policy, investment transactions (buys, sells, and exchanges) shall be made by means of a bid process when practicable to do so. Records of all offers/bids shall be maintained by investment personnel and recorded on an investment worksheet. When rapid moves in interest rates are occurring, transactions may be executed using trade information provided by the Bloomberg system.
- d. All payments for services rendered are paid from the Department's Power or Water Revenue Fund, as applicable.

2. OVERSIGHT

- a. All investment transactions will be reviewed monthly by the Assistant CFO and Treasurer or his/her designee for control purposes.
- b. Independent verification shall be performed by the Department's Accounting Section in connection with their reconciliation of monthly bank statements and fund balances.



3. EXCEPTIONS HANDLING AND REPORTING

Exceptions to the limits established in the Investment Policy shall be initially reported by investment personnel to the Investment Manager using the Exceptions Handling and Reporting Template within five business days of discovery. The Investment Manager shall review exception reports and determine the need to escalate the reporting of exceptions to internal audit or management. Exceptions shall be reported to the Board as part of the Quarterly Investment Report and to the Investment Committee in the annual Investment Committee Meeting. Exceptions to be reported shall include, but not be limited to, the following types:

- Authorized Investments - Any exceptions to the limitations to the type, percentage, maturity, rating, issuer, or other criteria specified in the Investment Policy
- Competitive Bidding – Any exception to the competitive bidding process specified in the Investment Policy.
- Collateral Requirements – Any exceptions to the collateral requirements specified in the Investment Policy.
- Safekeeping – Any exceptions to the safekeeping policy specified in the Investment Policy.
- Issuer Default – A default by an issuer of securities held in the portfolios
- Securities Lending - Any exceptions to the Securities Lending Policy, including, but not limited to the following:
 - Collateralization
 - Mark to Market
 - Matched vs. Mismatched Loans
 - Duration of Loans
 - Securities Available for Loan
 - Securities Lending Income
 - Indemnification of Losses
 - Authorized Investments of Cash Collateral
- Broker/Dealer – Any transactions with an unauthorized broker/dealer.



XVI. TRUST FUNDS INVESTMENT PROCEDURES

Investment personnel shall comply with the following Investment Procedures:

1. PRELIMINARY ANALYSIS AND PREPARATION

- a. Review periodically the portfolio and discuss investment objectives, constraints, strategy, and cash flow needs.
- b. Study and review, on a continuing basis, the Wall Street Journal, Bloomberg's analyses of securities performance, current financial literature, and consult with investment experts concerning interest rate projections and events that may result in possible market changes.

2. INVESTMENT ACTIVITIES

- a. Receive information regarding contributions from Financial Planning and Scenario Development Section. Also, review portfolio printout for maturing investments.
- b. Consider factors listed in preliminary analysis and preparation to determine the sector, amount, and term of the investment.
- c. Contact at least three dealers/brokers to obtain investment rates, to the extent practicable.
- d. Review description of investment offers/bids and calculate yield in Bloomberg.
- e. Record offers/bids received on the investment worksheet for documentation.
- f. Select dealer/broker with best offer or bid.
- g. Record selected offer or bid on the investment worksheet.
- h. Finalize purchase or sale with the broker/dealer and confirm wire instructions.
- i. Print yield analysis and security description in Bloomberg.
- j. Receive trade confirmation ticket from broker/dealer through Bloomberg and review for accuracy.



- k. Attach Bloomberg printouts, confirmation and other supporting documents to investment worksheet.
- l. Fax or e-mail the investment worksheet to Trustee or phone to Trustee details of each purchase or sale transaction such as:
 - 1. Broker's Name
 - 2. Security Description
 - 3. Amounts (Par, Cost, Accrued Interest, if any)
 - 4. Fund and Account Numbers
 - 5. Maturity Date
 - 6. Settlement Date
 - 7. Rates
 - 8. Wire Instructions
- m. Update investment in portfolio in Bloomberg and print portfolio trade ticket.
- n. Input to portfolio management software, all required information such as:
 - 1. Investment Worksheet Reference Number
 - 2. Account Number
 - 3. Type of Security
 - 4. Cusip
 - 5. Issuer
 - 6. Date of Purchase
 - 7. Issue Date
 - 8. Maturity Date
 - 9. Purchase Price
 - 10. Yield to Maturity/Call
 - 11. Coupon Rate
 - 12. Income Due on Interest Payment Dates
 - 13. Inter-fund Transfers of Income
 - 14. Accrued Interest Purchased
 - 15. Par Amount
 - 16. Cost
 - 17. Premium [Discount]
 - 18. Credit Rating
 - 19. Last Date Interest was Paid Immediately Prior to Purchase
 - 20. Broker Information.



- o. Print purchase/sale tickets.
- p. Compare electronic trade confirmation received from broker with trade tickets from Bloomberg and portfolio management software to ensure correctness.
- q. Receive confirmation of investment transaction by mail from brokers, typically one week after transaction.
- r. Compare transaction confirmation notices from investment firm with the purchase/sale tickets to ensure correctness.
- s. File confirmation notices and investment worksheet in completed investment file.
- t. Forward copy of investment worksheets, purchase/sales tickets and a copy of the investment portfolio monthly to the Assistant CFO and Treasurer or his/her designee.
- u. Confirm weekly transactions/activities and account balance with Trustee's records.
- v. Receive monthly bank statement from Trustee, typically one to three business days after month-end.
- w. Reconcile investment portfolio with monthly bank statement.
- x. Prepare monthly investment report that lists each investment (security) by fund and account number at par amount, cost, current market value and yield. The report will also include interest received, premium or discount, interest accrued as of the specific reporting month and portfolio performance.
- y. Submit monthly report for review and approval by the Assistant CFO and Treasurer or his/her designee.
- z. Send copy of monthly report to the Department's Accounting Section.
- aa. Prepare quarterly investment report that lists portfolio and benchmark yields, weighted cost of debt, if applicable, rate of return, investment cost, market value, modified and benchmark duration, weighted average life, and portfolio structure and composition by market sector, maturity and asset credit rating.
- bb. Prepare cover letter to Board of Water and Power Commissioners summarizing the investment results for the reporting period.



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- cc. Submit quarterly report and cover letter for review and approval by the Assistant CFO and Treasurer or his/her designee.
- dd. Submit quarterly report and cover letter to the Board of Water and Power Commissioners.