

FUNCTION: Short-Term Investments
ACTIVITY: Portfolio Rules

POLICY: The Oregon Investment Council has, with advice from the Treasurer, from OST investment staff, and from the Oregon Short-Term Fund Board, adopted specific rules for investing the Oregon Short-Term Fund (OSTF). These rules are included as sample form A.

PROCEDURES:

1. **Verify Compliance With Portfolio Rules.** The Senior Fixed Income Investment Officer and Investment Officer(s) receive an Oregon Short-Term Fund Daily Compliance Report. This report summarizes OSTF holdings by type of investment (asset allocation), by investment issuer, by time until investment maturity, and by investment quality (rating). The Daily Compliance Report also summarizes each Portfolio Rule as an "Objective," and compares the actual current portfolio to the objectives. The OSTF staff reviews this report, daily, to ensure compliance with portfolio rules.
2. **Oversight of Compliance.** The Deputy State Treasurer, Chief Investment Officer, Chief Audit Executive, Risk & Compliance Officer, and Investment Accounting staff receive and review this same report daily. For meetings at which the OSTF is discussed, the Oregon Short-Term Fund Board and the Oregon Investment Council receive and review the compliance report.
3. **Correction of Non-Compliance.** If the OSTF is found to be out of compliance with one or more adopted portfolio rules, the Senior Fixed Income Investment Officer or Investment Officer(s) shall sell (or purchase) the securities necessary to bring about compliance as soon as is prudently feasible.

SAMPLE FORMS, DOCUMENTS, OR REPORTS (Attached):

- A. Oregon Short-Term Fund Portfolio Rules
- B. Portfolio Compliance Report

Sample Form A

Oregon Short-Term Fund Portfolio Rules

These are the most current Portfolio Rules for the Oregon Short-Term Fund which have been adopted by the Oregon Investment Council.

Portfolio Rules For The Oregon Short-Term Fund

Amended April 27, 2011

I. Scope

These rules apply to the investment of cash from all state and eligible local government participants of the Oregon Short-Term Fund (“OSTF”). These rules are established under the authority of, and shall not supersede the requirements established under, ORS Chapter 293.

II. Investment Objectives

The primary objectives of investment activities, in priority order, shall be preservation of principal, liquidity, and yield.

- A. Preservation of Principal: Safety is the foremost objective of the OSTF rules. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk and interest rate risk (see specific guidelines below).
- B. Liquidity: The OSTF shall remain sufficiently liquid to meet all state agency and local government operating requirements that may be reasonably anticipated. This is accomplished by structuring the OSTF so that securities mature concurrent with cash needs to meet anticipated demands. Furthermore, since all possible cash demands cannot be anticipated, the OSTF should consist largely of securities with active secondary or resale markets.
- C. Yield: The OSTF 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 majority of the OSTF is limited to highly rated/low risk securities in anticipation of earning a fair return relative to the risk being assumed.

III. Standards of Care

- A. Prudence: The standard of prudence to be used by investment officers shall be the “prudent investor” standard and shall be applied in the context of managing the OSTF as a whole. Pursuant to ORS Chapter 293.726:

- (1) The investment funds shall be invested and the investments of those funds managed as a prudent investor would do, under the circumstances then prevailing and in light of the purposes, terms, distribution requirements and laws governing each investment fund.
 - (2) The standard stated in subsection (1) of this section requires the exercise of reasonable care, skill and caution, and is to be applied to investments not in isolation but in the context of each investment fund's investment portfolio and as a part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the particular investment fund.
- B. Ethics and Conflicts of Interest: Officers 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. Officers and employees shall, at all times, comply with the State of Oregon Government Standards and Practices code of ethics set forth in ORS Chapter 244, as well as all policies of the OST.
- C. Delegation of Authority: The Senior Investment Officer and Investment Officer(s) (or the Investment Analyst acting under the direction of the Investment Officers) shall act in accordance with established written procedures and internal controls for the operation of the investment program consistent with these Portfolio Rules. No person may engage in an investment transaction except as provided under the terms of these Portfolio Rules and the procedures established by OST staff. The Senior Investment Officer and Investment Officer(s) are jointly responsible for all transactions undertaken, and shall establish a reasonable system of controls to regulate the activities of subordinate employees.

IV. Safekeeping and Custody

- A. Authorized Financial Dealers and Institutions: All financial institutions and broker/dealers who desire to become qualified for investment transactions must supply, as appropriate:
- (1) Audited financial statements
 - (2) Licensing Representation form provided by OST
 - (3) Understanding and acknowledgement of OSTF Portfolio Rules located at <http://www.ost.state.or.us/About/Investment/>
- B. Internal Controls: The Senior Investment Officer and Investment Officer(s) jointly collaborate to establish and maintain an adequate internal control structure designed to reasonably protect the assets of the OSTF from loss, theft or misuse.

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

V. Maturity Distribution of Portfolio

- A. 50% of the portfolio must mature within 93 days.
- B. A maximum of 25% of the portfolio may mature over one year.
- C. No investment may mature in over 3 years as measured from settlement date. The OSTF Daily Compliance Report adheres to trade date accounting, thus creating potential short term exceptions on the Daily Compliance Report when a “new issue” 3-year security is purchased. Any such securities will be disclosed on the Daily Compliance Report, when purchased.
- D. For securities that have been called by the issuer, the effective call date will be used as a proxy for the maturity date.
- E. For variable rate securities, the period remaining to the next reset date will be used as a proxy for the maturity date.

VI. Diversification and Limitations of Portfolio

- A. Eligible Securities:
 - (1) U.S. Treasury Securities
 - a. 100% of the portfolio may be in U.S. Treasury securities.
 - (2) Senior unsecured debt obligations guaranteed by the Federal Deposit Insurance Corporation (FDIC) under the Temporary Liquidity Guarantee Program (TLGP); Eligible TLGP debt obligations carry the full faith and credit of the United States.
 - a. 50% maximum of portfolio per FDIC-guarantee exposure.
 - (3) U.S. Government Agency Securities
 - a. 100% of the portfolio may be in U.S. Government Agency securities.
 - b. 33% maximum of portfolio per agency issuer.
 - For newly issued Agency securities, and absent assigned ratings, “expected ratings” may be used as a proxy for assigned ratings for not more than 30 business days after the anticipated settlement date.

- (4) Foreign Government Securities and their Instrumentalities
 - a. 25% maximum of portfolio in foreign government securities and their instrumentalities.
 - b. 10% maximum of portfolio per issuer.
 - c. Foreign government securities must have minimum long-term ratings of AA-, Aa3, or AA-, or better, by Standard & Poor's, Moody's Investors Services, or Fitch Ratings, respectively, at the time of purchase.

- (5) Corporate Indebtedness
 - a. 50% maximum of portfolio in corporate indebtedness.
 - b. 5% maximum of portfolio per issuer in commercial paper and corporate notes.
 - c. Commercial Paper (CP) must have top-tier short term ratings by at least two of the following nationally recognized statistical rating organizations (NRSRO) at the time of purchase (Standard & Poor's = minimum A-1, Moody's Investors Services = minimum P-1, Fitch Ratings = minimum F1).
 - d. Corporate notes must have minimum long-term ratings of A-, A3, or A-, or better, by Standard & Poor's, Moody's Investors Services, or Fitch Ratings, respectively, at the time of purchase.
 - For newly issued corporate securities, and absent assigned ratings, "expected ratings" may be used as a proxy for actual ratings for not more than 30 business days after the anticipated settlement date.
 - e. 25% maximum of portfolio in total foreign exposure (government and corporate indebtedness)

- (6) Negotiable Certificates of Deposit (NCD's)
 - a. 20% maximum of portfolio in NCD's.
 - b. 5% maximum of portfolio per issuer in domestic bank NCD's.
 - c. NCD's must have minimum ratings of AA-, Aa3, or AA-, or better, by Standard & Poor's, Moody's Investors Services, or Fitch Ratings, respectively, at the time of purchase.

- (7) Bankers' Acceptances (BA's)
 - a. 20% maximum of portfolio in BA's.
 - b. 5% maximum of portfolio per issuer in domestic bank BA's
 - c. BA's must have minimum ratings of AA-, Aa3, or AA-, or better, by Standard & Poor's, Moody's Investors Services, or Fitch Ratings, respectively, at the time of purchase.

- (8) Time Certificates of Deposit (TCD's)
 - a. 20% maximum of portfolio in TCD's.
 - b. Permitted TCD's will be limited to qualified depositories as defined in ORS Chapter 295.005.

- c. Maximum TCD exposure per depository must be no more than 5% of the bank's total deposits, or \$100,000, whichever is greater. Maximum credit union exposure per depository shall be \$100,000.
- (9) Municipal Debt
 - a. Municipal debt obligations (agencies, instrumentalities, and political subdivisions) that have long-term ratings of AA-, Aa3 or AA-, or better, or are rated in the highest category for short-term municipal debt by Standard & Poor's, Moody's Investors Services, or Fitch Ratings, respectively, at the time of purchase.
 - (10) Repurchase Agreements
 - a. Maximum maturity will be 90 days.
 - b. Net capital of counterparty must be greater than \$100 million.
 - c. Repurchase Agreements must equal no more than 2% of liabilities of the counterparty.
 - d. No more than 5% of OSTF assets shall be placed with the same counterparty for repurchases.
 - e. Counterparty must be a Primary Dealer as recognized by the Federal Reserve Bank. The only exception is OST's custodial agent as a non-primary dealer counterparty.
 - f. The counterparty must have a signed repurchase agreement.
 - g. Collateral must be delivered to the OST's account at its custodian or to an account established for the OST pursuant to the terms of the specific Repurchase Agreement in the name of the Office of the State Treasurer.
 - h. Collateral for repurchase agreements may be U.S. Treasury or U.S. Agency Discount and Coupon securities only. Collateral must have a final maturity of three years or less. The market value of the delivered collateral must be maintained at not less than 102% of the cash invested.
 - (11) Reverse Repurchase Agreements
 - a. Maximum maturity will be 90 days.
 - b. Net capital of counterparty must be greater than \$100 million.
 - c. Reverse Repurchase Agreements must equal no more than 2% of liabilities of the counterparty.
 - d. No more than 5% of OSTF assets shall be placed with the same counterparty for reverse repurchase agreements.
 - e. Counterparty must be a Primary Dealer as recognized by the Federal Reserve Bank.
 - f. The counterparty must have a signed repurchase agreement.
 - g. Acceptable reinvestment vehicles include securities that may otherwise be purchased outright.
 - h. Securities will be reversed on a fully collateralized basis.

- i. Reverse repurchase investments for interest rate arbitrage shall only be done on a matched book basis.
- B. All portfolio investments will be denominated in US\$ only.
- C. 10% maximum of portfolio per issuer on all securities and support commitments with the exception of U.S. Treasury (100% maximum) and Government Agency securities (33% per issuer).
- D. Securities that have been downgraded to below the minimum ratings will be sold or held at the Senior Investment Officer’s (SIO) discretion. In the absence of the SIO, or if the SIO is inaccessible, Investment Officer(s) will have discretion to sell or hold the downgraded securities. Such securities will be disclosed in the OSTF Daily Compliance Report and actively monitored by OST staff. The Senior Investment Officer, or the Investment Officer(s), is responsible for bringing the OSTF back into compliance as soon as is practicable.
- E. A single rating will be determined for each investment based on the methodology:

To determine rating for each investment:

- i. When three NRSROs rate an issue, a median rating is used to determine eligibility by dropping the highest and/or lowest rating.
- ii. When a rating from only two NRSROs is available, the lower (“most conservative”) of the two is used.
- iii. When a rating from only one NRSRO is available, that rating is used.

To determine average rating for each security, a numeric value will be assigned to each nationally recognized statistical rating organization’s (NRSRO) rating based the following scheme:

Value	Moody’s Ratings		S&P Ratings		Fitch Ratings	
	Long Term	Short Term	Long Term	Short Term	Long Term	Short Term
1	US Treasury		US Treasury		US Treasury	
1	Agency		Agency		Agency	
1	Aaa		AAA		AAA	
2	Aa1		AA+		AA+	
3	Aa2		AA		AA	
4	Aa3	P-1 ¹	AA-	A-1+	AA-	F-1+
5	A1	P-1	A+	A-1	A+	F-1
6	A2		A		A	
7	A3	P-2	A-	A-2	A-	F-2
8	Baa1		BBB+		BBB+	
9	Baa2		BBB		BBB	
10	Baa3		BBB-		BBB-	

- F. The target weighted average credit quality of the portfolio shall be < 3.50).

- G. No commitments to buy or sell securities may be made more than 14 business days prior to the anticipated settlement date, or receive a fee other than interest for future deliveries.

VII. Securities Lending for Reinvestment of Cash Collateral

- A. Acceptable reinvestment vehicles include securities that may otherwise be purchased outright in accordance with the Portfolio Rules for the Oregon Short-Term Fund (Sections VI). Within the securities lending program only, cash collateral may also be reinvested in:
 - (1) Maximum of 15% in asset backed securities rated AAA/Aaa, limited to auto loan and credit card issues with an average life of three years or less.
 - (2) Maximum of 25% in A, or higher, rated corporate floating rate notes with a maximum final maturity of three years, and fixed rate corporate notes with a maximum final maturity of two years; up to 65% maximum in corporate indebtedness including commercial paper.
 - (3) Repurchase agreements collateralized by U.S. Treasury or U.S. Government Agency securities with a maximum original maturity of 30 years. No more than 25% of assets shall be placed with the same counterparty.
 - (4) All Repurchase Agreements (under the Special Indemnification by State Street clause) must be fully collateralized by collateral, determined by State Street in its discretion, limited to the following: U.S. Treasuries, U.S. Treasury STRIPS, Federal Agency Obligations, Corporate securities rated A- or higher, Asset-Backed Securities rated A- or higher, Agency MBS pass throughs rated AAA, Commercial Paper rated A-1/P-1 or higher, or any combination thereof.² For purposes of calculating average credit quality, current ratings of the indemnifier, State Street Corp, will be used.
 - (5) The target weighted average credit quality shall be < 3.8 by Standard & Poor's or Moody's Investors Services.
- B. Net capital of lending counterparty must be over \$100 million.
- C. Securities will only be loaned on a fully collateralized basis.
- D. Lending counterparty must be a Primary Dealer as recognized by the Federal Reserve Bank, and have a signed master securities lending agreement.
- E. The market value of the delivered collateral must be maintained at not less than 102% of the market value of the securities loaned.

- F. Reverse Repurchase Agreements are prohibited within the securities lending program.
- G. 25% of the reinvestment portfolio must mature within 93 days; up to 50% of the portfolio may mature in over one year.

¹ Unlike S&P, Moody's does not differentiate short term ratings with a plus (+), which indicates that the obligor's capacity to meet its financial commitment on these obligations is extremely strong. As such, in terms of average credit quality valuation, Moody's short term ratings/valuations will correspond to the lowest S&P short term ratings/valuations.

² Special Indemnification of Client By State Street: Notwithstanding any provision herein to the contrary, if the value of the Liquidation Proceeds under Reverse Transactions (entered into between State Street (as agent for the Client) and a counterparty in respect of whom an event of default has occurred under the agreement governing such Reverse Transactions) is less than the cash to be delivered by that counterparty under such Reverse Transactions on the date of close-out of the same, State Street shall indemnify the Client for any such difference. The term "Liquidation Proceeds" means the market value of the securities used to collateralize the Reverse Transaction(s) on the date that State Street takes action with respect to such securities under the applicable agreement. The term "Reverse Transactions" means each transaction entered into between the Client and a counterparty (through the agency of State Street) under the terms of an agreement pursuant to which the counterparty initially transfers securities to the Client and the Client transfers cash to the counterparty. All of such Reverse Transactions will be entered into in connection with the investment of cash Collateral received from Borrowers in connection with Loans hereunder."