LOS ANGELES UNIFIED SCHOOL DISTRICT
INVESTMENT POLICY

Statement of Investment Policy

The investment objective of the District is to invest public funds in a manner which will maximize the investment return on all of its funds with maximum security while meeting the daily cash flow demands of each portfolio of the District and conforming to all Federal, State, and local statutes governing the investment of public funds.

Investment Objectives

Safety

- Safety is the foremost objective of the investment program. All Investments of the District shall be undertaken to ensure the preservation of capital in the overall portfolio. To attain this objective, the District will diversify its investments by investing funds among a variety of securities offering independent returns and financial institutions.

Liquidity

- The District's investment portfolios will remain sufficiently liquid to enable the District to meet its operating requirements which might be reasonable anticipated.

Return on investment

- The District's Investment portfolios shall be structured to attain a maximum return commensurate with its investment risk constraints and the cash flow characteristics of each portfolio.

Designation of Investment Officer

The District's Chief Financial Officer (CFO) and Controller, together with such member(s) of their staffs as they may designate by express written authorization or who may be acting from time to time subject to express direction by the CFO or Controller, will hereafter be referred to collectively in these Investment Policy as the District's Investment Officer. The Investment Officer will invest or cause to be invested the Investable Funds of the District in accordance with these Investment Policy.

Cash Flow Forecasting

During each fiscal year, the District's Controller will, as frequently as is necessary, prepare or cause to be prepared cash flow forecasts for each of the District's funds for purposes of estimating (1) the timing and magnitude of District expenditures, and (2) the aggregate amount of District Investable Funds.

Basic Investment Practice

The District's Investment Officer, acting in consultation and cooperation with the Los Angeles County Treasurer's Office, will cause the District's Investable Funds to be invested in "Authorized Investment Securities" (as defined hereafter) maturing not later than the date or dates indicated in the District's current cash flow forecast as requiring funds to be available for expenditure. The Investment Officer may take into account differences in yield and other market factors when evaluating specific proposed investments. The Investment Officer may cause Investable Funds to be invested to shorter maturity dates if securities market conditions appear to warrant such action and may not cause Investable Funds to be invested with maturities beyond the date(s) forecast for expenditure of such funds. As used in these Investment Policy, the term "maturity" means the stated final maturity of a security.

Generally, the Investment Officer should be attempting to maximize the yield on the investments over the available life of the investable funds subject to the maturity constraint in this section and the authorized securities Policy in the next section. However, relative value on a risk adjusted basis may also be considered if market conditions warrant. Also, for any sizeable specific investments it will be considered good practice to generally ladder maturities throughout the expected availability horizon to limit the impact of market interest rate moves and to mitigate impacts of unexpected changes in cash requirements.

This investment policy applies to all financial assets of the District. These funds are report in the District's Comprehensive Annual Financial Report and include:

- General Fund
- Workers Compensation Fund
- PARS
- Capital Funds
    - General Obligation Bonds
    - Certificates of Participation
    - QZABs
    - TRANS
    - PARS
- And any other fund unless specifically exempted.

All investments shall be made with judgment and care – under circumstances then prevailing – which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

Authorized Investment Securities

Authorized Investment Securities are securities in which investment is allowed by or on behalf of the District by state law, subject to any additional restrictions or limitations set forth in these Investment Policy. Authorized Investment Securities include, but are not limited to:

A. U.S. Treasury securities. Up to 100% of Investable Funds may be invested in securities issued by U.S. Treasury, with maturities not exceeding the shorter of the statutory maximum (as defined in Government Code Section 53601) and the anticipated date(s) of expenditure of such funds.

B. Obligations (1) issued by agencies or instrumentalities of the United States; (2) guaranteed by the United States or an agency or instrumentality thereof; or (3) issued or guaranteed by a U.S. government sponsored enterprise, including, but not limited to, the Federal Farm Credit System, the Federal Home Loan Bank System, the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, and the Student Loan Marketing Association. Up to 75% of Investable Funds may be invested in such obligations.

Obligations of any one issuer may not exceed 25% of aggregate Investable Funds. Maturities may not exceed the shorter of the statutory maximum and the anticipated date(s) of expenditure of Investable Funds. Obligations issued by an agency or instrumentality of the United States or by a U.S. government sponsored enterprise and which mature in less than one year should yield a minimum of 5 basis points (0.05%) more than comparably maturing U.S. Treasury securities. Such securities maturing in 1-3 years should yield at least 10 basis points (0.10%) and those maturing in 3-5 years should yield at least 15 basis points (0.15%) more than comparably maturing U.S. Treasury securities. Such securities maturing beyond 5 years, and all securities guaranteed by the United States or by an agency or instrumentality thereof, should yield at least 25 basis points (0.25%) more than comparably maturing U.S. Treasuries. Mortgage-backed obligations should yield at least 37.5 basis points (0.375%) more than the U.S. Treasury security maturing closest to the average life of each mortgage-backed obligation; provided that such average life is computed assuming a prepayment speed generally in line with the Bloomberg dealer consensus speed applicable to the mortgage collateral securing each mortgage-backed obligation.

C. Other investment securities permitted to the District by statute, including, but not limited to, obligations issued by (1) corporations, including but not limited to, commercial paper, medium term notes, or other corporate indebtedness; and (2) financial institutions, including, but not limited to, commercial paper, certificates of deposit, bankers acceptances, medium term notes, or deposit notes. No more than 50% of aggregate Investable Funds may be invested in the obligations of any one issuer or related entity. Maturities may not exceed the shorter of the statutory maximum and the anticipated date(s) of expenditure of Investable Funds. Ratings must meet or exceed statutory minimums. As a general rule, such obligations are more appropriate for shorter-term investments than for longer maturities.

Securities purchased under authority of this paragraph and which mature in less than one year should yield more than 15 basis points (0.15%) above comparably maturing U.S. Treasury obligations. Securities maturing beyond one year should yield not less than 50 basis points (0.50%) above comparably maturing U.S. Treasuries.

For securities covered by this section, information pertaining to the issuer's financial position and its ability to repay obligations should be obtained, reviewed and maintained in file prior to purchase and on an at least annual basis thereafter until maturity. This credit evaluation function may be performed by the Investment Officer or provided by an independent outside party such as the County Investment Department.

D. Pooled investments managed by the Los Angeles County Treasurer's Office. Up to 100% of Investable Funds may be invested in this manner. Issuer concentration limits specified in paragraphs B & C above do not apply to, or limit the District's use of, pooled investments, irrespective of the composition of such pooled investments from time to time. The Investment Officer may use pooled investments either as a substitute for other specific securities or as a repository for that portion of Investable Funds for which it is difficult to forecast a specific expenditure date or both.

When pooled investments are used as a substitute for specific securities, the expected yield should be in excess of 12.5 basis points (0.125%) above comparably maturing U.S. Treasury obligations, computed against the dollar weighted average life of the pooled instruments. Pooled investments should also be used where the incremental yield on specific investments is not sufficient to compensate for lost revenue from float income tied to the pool balance.

Whenever investing in any Los Angeles County pool(s), the Investment Officer should obtain and review the most recent financial statement for the pool(s). Particular attention should be paid to the portfolio composition and whether the resulting credit, liquidity, and interest rate sensitivity aspects are consistent with the LAUSD investment practice as stated above. While participating on an ongoing basis, quarterly pool reports should also be so reviewed.

Exceptions

Any exceptions to this policy must be approved by the Board of Education of the Los Angeles Unified School District.

Reporting of Investment Activity

The Investment Officer will report investment activity to the BFAT Committee annually at the conclusion of the fiscal year. Reports will include, but not necessarily be limited to, a list of securities purchased, sold, or matured since the last report; the current composition of investments and the yields and maturities thereof; and a brief review of current market conditions and investment strategy.

Recordkeeping Audits

The Investment Officer will keep current detailed and accurate records of all transactions involving Investable Funds to facilitate auditing by internal and external auditors.

Annual Review of Investment Policy

Prior to the beginning of each new fiscal year the BFAT Committee will review current Investment Policy, request any changes which may be necessary or proper, and approve Investment Policy which will apply to the forthcoming fiscal year. The date of approval of these Investment Policy, which apply to fiscal year 2005-06, is upon adoption of this report by the District's governing board.

Investment Portfolios

General Obligation Bonds

COPS

QZABs

TRANS

Workers Commensuration

PARS

Investment Procedures
Ethics and Conflicts of Interest
Master Purchase Agreements
Investment Pools/Mutual Funds
Collateralization
Funding of Treasure Functions

APPENDIX A

California Government Code Update
(As of January 2005)

A summary of changes and additions to California Government Code Sections 53601, 53630, and 53646 is provided below:

Section 53601

- 53601(o): This new subdivision adds eligibility criteria for investing in JPA pools. The JPA issuer must retain an investment advisor who is registered with the Securities and Exchange Commission (or exempt from registration), has assets under management in excess of $500 million, and has at least five years experience investing in instruments authorized by Government Code Section 53601(a) – (n).
- 53601.7(a): This section adds a securities lending agreement as one of the agreements under which an investment may be made in a security.
- 53601.2: This new section defines "corporation" as a limited liability company.

Section 53630

- 53630(j): This new subdivision defines "corporation" as a limited liability company.

Section 53646

- 53646(a): This subdivision has been revised to remove the annual mandatory filing of a local agency's annual investment policy. This section now provides the treasurer of a county government or the treasurer or chief fiscal officer of any other local agency the option of submitting an annual investment policy to his/her legislative body and any oversight committee.
- 53646(b): This subdivision has been **revised to remove the mandatory filing** of a local agency's quarterly investment report. This section now provides the treasurer or chief fiscal officer of a local agency the option of submitting a quarterly investment report to the chief executive officer, the internal auditor, and the legislative body of the local agency.

APPENDIX B

GLOSSARY

AGENCIES: Federal agency securities and/or Government-sponsored enterprises.

ASKED: The price at which securities are offered.

BANKERS' ACCEPTANCE (BA): A draft or bill or exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the issuer.

BENCHMARK: A comparative base for measuring the performance or risk tolerance of the investment portfolio. A benchmark should represent a close correlation to the level of risk and the average duration of the portfolio's investments.

BID: The price offered by a buyer of securities. (When you are selling securities, you ask for a bid.) See Offer.

BROKER: A broker brings buyers and sellers together for a commission.

CERTIFICATE OF DEPOSIT (CD): A time deposit with a specific maturity evidenced by a Certificate. Large-denomination CD's are typically negotiable.

COLLATERAL: Securities, evidence of deposit or other property, which a borrower pledges to secure repayment of a loan. Also refers to securities pledged by a bank to secure deposits of public monies.

COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR): The official annual report for the *District*. It includes five combined statements for each individual fund and account group prepared in conformity with GAAP. It also includes supporting schedules necessary to demonstrate compliance with finance-related legal and contractual provisions, extensive introductory material, and a detailed Statistical Section.

COUPON: (a) The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value. (b) A certificate attached to a bond evidencing interest due on a payment date. DEALER: A dealer, as opposed to a broker, acts as a principal in all transactions, buying and selling for his own account.

DEBENTURE: A bond secured only by the general credit of the issuer.

DELIVERY VERSUS PAYMENT: There are two methods of delivery of securities: delivery versus payment and delivery versus receipt. Delivery versus payment is delivery of securities with an exchange of money for the securities. Delivery versus receipt is delivery of securities with an exchange of a signed receipt for the securities.

DERIVATIVES: (1) Financial instruments whose return profile is linked to, or derived from, the movement of one or more underlying index or security, and may include a leveraging factor, or (2) financial contracts based upon notional amounts whose value is derived from an underlying index or security (interest rates, foreign exchange rates, equities or commodities).

DISCOUNT: The difference between the cost price of a security and its maturity when quoted at lower than face value. A security selling below original offering price shortly after sale also is considered to be at a discount.

DISCOUNT SECURITIES: Non-interest bearing money market instruments that are issued a discount and redeemed at maturity for full face value, *e.g.*, U.S. Treasury Bills.

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

FEDERAL CREDIT AGENCIES: Agencies of the Federal government set up to supply credit to various classes of institutions and individuals, *e.g.*, S&L's, small business firms, students, farmers, farm cooperatives, and exporters.

FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC): A federal agency that insures bank deposits, currently up to $100,000 per deposit. FEDERAL FUNDS RATE: The rate of interest at which Fed funds are traded. This rate is currently pegged by the Federal Reserve through open- market operations.

FEDERAL HOME LOAN BANKS (FHLB): Government sponsored wholesale banks (currently 12 regional banks), which lend funds and provide correspondent banking services to member commercial banks, thrift institutions, credit unions and insurance companies. The mission of the FHLBs is to liquefy the housing related assets of its members who must purchase stock in their district Bank.

FEDERAL NATIONAL MORTGAGE ASSOCIATION (FNMA): FNMA, like GNMA was chartered under the Federal National Mortgage Association Act in 1938. FNMA is a federal corporation working under the auspices of the Department of Housing and Urban Development (HUD). It is the largest single provider of residential mortgage funds in the United States. Fannie Mae, as the corporation is called, is a private stockholder-owned corporation. The corporation's purchases include a variety of adjustable mortgages and second loans, in addition to fixed-rate mortgages. FNMA's securities are also highly liquid and are widely accepted. FNMA assumes and guarantees that all security holders will receive timely payment of principal and interest.

FEDERAL OPEN MARKET COMMITTEE (FOMC): Consists of seven members of the Federal Reserve Board and five of the twelve Federal Reserve Bank Presidents. The President of the New York Federal Reserve Bank is a permanent member, while the other Presidents serve on a rotating basis. The Committee periodically meets to set Federal

Reserve Policy regarding purchases and sales of Government Securities in the open market as a means of influencing the volume of bank credit and money.

FEDERAL RESERVE SYSTEM: The central bank of the United States created by Congress and consisting of a seven member Board of Governors in Washington, D.C., 12 regional banks and about 5,700 commercial banks that are members of the system.

GOVERNMENT NATIONAL MORTGAGE ASSOCIATION (GNMA or Ginnie Mae): Securities influencing the volume of bank credit guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loan associations, and other institutions. Security holder is protected by full faith and credit of the U.S. Government. Ginnie Mae securities are backed by the FHA, VA or FmHA mortgages. The term "pass-throughs" is often used to describe Ginnie Maes.

LIQUIDITY: A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of va lue. In the money market, a security is said to be liquid if the spread between bid and asked prices is narrow and reasonable size can be done at those quotes. LOCAL GOVERNMENT INVESTMENT POOL (LGIP): The aggregate of all funds from political subdivisions that are placed in the custody of the State Treasurer for investment and reinvestment.

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

MASTER REPURCHASE AGREEMENT: A written contract covering all future transactions between the parties to repurchase – reverse repurchase agreements that establishes each party's rights in the transactions. A master agreement will often specify, among other things, the right of the buyer-lender to liquidate the underlying securities in the event of default by the seller borrower.

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

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

OFFER: The price asked by a seller of securities. (When you are buying securities, you ask for an offer.) See Asked and Bid.

OPEN MARKET OPERATIONS: Purchases and sales of government and certain other securities in the open market by the New York Federal Reserve Bank as directed by the FOMC in order to influence the volume of money and credit in the economy. Purchases inject reserves into the bank system and stimulate growth of money and credit; sales have the opposite effect. Open market operations are the Federal Reserve's most important and most flexible monetary policy tool.

PORTFOLIO: Collection of securities held by an investor.

PRIMARY DEALER: A group of government securities dealers who submit daily reports of market activity and positions and monthly financial statements to the Federal Reserve Bank of New York and are subject to its informal oversight. Primary dealers include Securities and Exchange Commission (SEC)-registered securities broker-deale rs, banks, and a few unregulated firms.

PRUDENT PERSON RULE: An investment standard. In some states the law requires that a fiduciary, such as a trustee, may invest money only in a list of securities selected by the custody state – the so-called legal list. In other states the trustee may invest in a security if it is one which would be bought by a prudent person of discretion and intelligence who is seeking a reasonable income and preservation of capital.

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

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

REPURCHASE AGREEMENT (RP OR REPO): A holder of securities sells these securities to an investor with an agreement to repurchase them at a fixed price on a fixed date. The security "buyer" in effect lends the "seller" money for the period of the agreement, and the terms of the agreement are structured to compensate him for this. Dealers use RP extensively to finance their positions. Exception: When the Fed is said to be doing RP, it is lending money that is, increasing bank reserves.

SAFEKEEPING: A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank’s vaults for protection.

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

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

SEC RULE 15C3-1: See Uniform Net Capital Rule.

STRUCTURED NOTES: Notes issued by Government Sponsored Enterprises (FHLB, FNMA, SLMA, etc.) and Corporations, which have imbedded options (e.g., call features, step-up coupons, floating rate coupons, derivative-based returns) into their debt structure. Their market performance is impacted by the fluctuation of interest rates, the volatility of the imbedded options and shifts in the shape of the yield curve.

TREASURY BILLS: A non- interest bearing discount security issued by the U.S. Treasury to finance the national debt. Most bills are issued to mature in three months, six months, or one year.

TREASURY BONDS: Long-term coupon-bearing U.S. Treasury securities issued as direct obligations of the U.S. Government and having initial maturities of more than 10 years.

TREASURY NOTES: Medium-term coupon-bearing U.S. Treasury securities issued as direct obligations of the U.S. Government and having initial maturities from two to 10 years.

UNIFORM NET CAPITAL RULE: Securities and Exchange Commission requirement that member firms as well as nonmember broker-dealers in securities maintain a maximum ratio of indebtedness to liquid capital of 15 to 1; also called net capital rule and net capital ratio. Indebtedness covers all money owed to a firm, including margin loans and commitments to purchase securities, one reason new public issues are spread among members of underwriting syndicates. Liquid capital includes cash and assets easily converted into cash.

YIELD: The rate of annual income return on an investment, expressed as a percentage. (a) INCOME YIELD is obtained by dividing the current dollar income by the current market price for the security. (b) NET YIELD or YIELD TO MATURITY is the current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond.