



## INVESTMENT POLICY

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## **1. PURPOSE**

This Investment Policy is set forth by Eastern Municipal Water District (hereinafter referred to as "District") for the following purposes:

- a. To establish a clear understanding for the governing Board, management, responsible employees, citizens and third parties of the objectives, policies and guidelines for the investment of the District's idle and surplus funds;
- b. To offer guidance to investment staff and any external investment advisers on the investment of District funds; and

The District establishes investment policies that meet its current investment goals. The District shall review this policy annually and may change its policies as its investment objectives change.

## **2. SCOPE**

This investment policy applies to all investment activities and financial assets of the District, which includes the general fund, special revenue funds, debt service funds, capital project funds, enterprise funds, and internal service funds. This policy is generally applicable to bond proceeds with consideration given to specific provisions of each issuance. The District's Investment Policy does not apply to funds held in trust in the District's name in pension or other post-employment benefit accounts. The funds covered by this policy are accounted for and incorporated in the District's Annual Comprehensive Financial Report and reported monthly in the District's Treasurer's Report.

## **3. DELEGATION OF AUTHORITY**

Authority to manage the District's investment program is derived from California Government Code, Sections 41006 and 53600 *et seq.*

The Board of Directors, as permitted under California Government Code, Section 53607, delegates the responsibility to invest or reinvest the funds of the Eastern Municipal Water District to the Treasurer who shall be responsible for the management of the District's investments. If circumstances prevent the Treasurer from actively investing on behalf of the District, the Chief Financial Officer is authorized to invest during such period subject to the limitations described herein.

The Treasurer is responsible for the District's cash management, including the administration of this investment policy, receiving and depositing monies of the District, and the certification that checks presented for Board approval in payment of obligations of the District are correct and supporting documents are available. Such procedures will include explicit delegation of authority to internal staff responsible for investment transactions. No person may engage in an investment transaction except as provided

under the terms of this policy and the procedures established by the Treasurer.

The District may engage the services of one or more external investment advisers, who are registered under the Investment Advisers Act of 1940, to assist in the management of the District's investment portfolio in a manner consistent with the District's objectives. External investment advisers may be granted discretion to purchase and sell investment securities in accordance with this investment policy.

The District's overall investment program shall be designed and managed with a degree of professionalism that is worthy of the public trust. The District recognizes that in a diversified portfolio, occasional measured losses may be inevitable and must be considered within the context of the overall portfolio's return and the cash flow requirements of the District.

#### **4. PRUDENT INVESTOR STANDARD**

In accordance with Government Code 53600.3, the District Treasurer and internal staff, responsible for managing the day-to-day tasks of the investment portfolio, are fiduciaries subject to the "Prudent Investor Standard" which shall be applied in the context of managing the overall portfolio. When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, District staff shall act with care, skill, prudence, and diligence to meet the objectives set forth in the Policy to safeguard investment principal, maintain liquidity needs of the District, and earn a reasonable competitive market rate of return.

#### **5. ETHICS AND CONFLICTS OF INTEREST**

Staff responsible for managing the investment portfolio shall refrain from personal business activity that could conflict with proper execution and management of the Policy and the investment program, or which could impair their ability to make impartial decisions. Staff shall disclose to the District and on the annual Statement of Economic Interest Form any material financial interest in financial institutions that conduct business with the District. Staff must refrain from undertaking personal investment transactions with the same individual(s) employed by the financial institution with whom business is conducted on behalf of the District.

#### **6. INTERNAL CONTROLS**

The Treasurer shall establish and maintain internal controls designed to ensure that the assets of the District are protected from loss, theft, fraud, and misuse.

Accordingly, the Treasurer shall establish an annual process of independent review by an external auditor. The annual audit will provide internal controls by assuring compliance with policies and procedures.

## **7. AUTHORIZED FINANCIAL INSTITUTION, DEPOSITORIES, AND BROKER DEALERS**

To the extent practicable, the Treasurer shall endeavor to complete investment transactions using a competitive bid process whenever possible. The Treasurer will determine which financial institutions are authorized to provide investment services to the District. It shall be the District's policy to purchase securities only from authorized institutions and firms.

The Treasurer shall maintain procedures for establishing a list of authorized broker/dealers and financial institutions which are approved for investment purposes that are selected through a process of due diligence as determined by the District. Due inquiry shall determine whether such authorized broker/dealers, and the individuals covering the District are reputable and trustworthy, knowledgeable and experienced in Public Agency investing and able to meet all of their financial obligations. These institutions may include "primary" dealers or regional dealers that qualify under Securities and Exchange Commission (SEC) Rule 15c3-1 (uniform net capital rule) and California Government Code, Section 53601.5.

Selection of broker/dealers used by an external investment adviser retained by the District will be at the sole discretion of the adviser with oversight from the District's staff. At least annually, the District's staff will request a list of the external advisor's approved broker/dealers and a summary of the process used in their due diligence of the approved broker/dealers. Where possible, transactions with broker/dealers shall be selected on a competitive basis and their bid or offering prices shall be recorded. If there is no other readily available competitive offering, best efforts will be made to document quotations for comparable or alternative securities. When purchasing original issue instrumentality securities, no competitive offerings will be required as all dealers in the selling group offer those securities at the same original issue price.

All financial institutions which desire to become qualified bidders for investment transactions (and which are not dealing only with the investment adviser) must supply the Treasurer with audited financials and a statement certifying that the institution has reviewed the California Government Code, Section 53600 *et seq.* and the District's investment policy. The Treasurer will conduct an annual review of the financial condition and registrations of such qualified bidders.

Public deposits will be made only in qualified public depositories as established by State law. Deposits will be insured by the Federal Deposit Insurance Corporation, or, to the extent the amount exceeds the insured maximum, will be collateralized in accordance with State law.

## 8. STATEMENT OF OBJECTIVES

The primary objective of this policy shall be safeguarding principal when investing public funds. The second objective shall be meeting all liquidity requirements and the third objective shall be achieving an acceptable return on investments. In order of priority, three fundamental criteria shall be followed in the investment program:

1. **Safety of Principal** – Investments shall be undertaken in a manner which first seeks to ensure the preservation of principal in the portfolio. Each investment transaction shall be entered into after taking into consideration the quality of the issuer, the underlying security or collateral, and diversification of the portfolio. Market risk shall be reduced by performing continuous cash flow analysis to avoid the need to sell securities prior to maturity.
2. **Liquidity** – In an effort to ensure the District’s portfolio will be sufficiently liquid to meet current and anticipated operating requirements, a cash flow analysis will be performed on an ongoing basis. Investments shall be made so that the maturity date is compatible with cash flow needs and safety of principal.
3. **Return on Investment** – Investments shall be undertaken to produce an acceptable rate of return after first considering safety of principal and liquidity and the prudent investor standard.

The portfolio will be managed to meet the District’s cash flow needs. All investment activity shall be consistent with the prudent investor standard (Section 3) and in accordance with the authorized investments (Section 9) included in this policy.

## 9. AUTHORIZED INVESTMENTS

The District is authorized by Government Code, Sections 53601, 53635, and 53684, to invest District funds in specific types of securities. Investments not listed in the below table, Allowable Investment Instruments Per State Government Code Applicable to All Local Agencies, are prohibited. The Treasurer may invest in any security authorized for investment under the state law or indenture, subject to the limitations described herein.

### Maturity Limitations

Instruments shall mature within five years from the settlement date unless the Board authorizes a longer term before the investment is made, in accordance with Government Code, Section 53601.

### Sale of Securities

Securities may be sold to provide needed liquidity, to restructure the portfolio to reduce risk, or to increase the expected return of the portfolio. In no instance shall a sale of

securities be for speculative purposes.

#### Portfolio Adjustments

Portfolio percentage limitations for each category of investment is applicable only at the date of purchase. Should an investment percentage of portfolio limitation be exceeded due to an incident such as a fluctuation in portfolio size, the Treasurer is not required to sell the affected securities. The Treasurer shall review the portfolio monthly or when credit or market circumstances dictate and report any instances of noncompliance to the Board of Directors.

Should a security held in the portfolio be downgraded below the minimum criteria included in this Statement of Investment Policy, the Treasurer shall determine whether the security shall be held or sold based on the economic outlook of the issuer, current market conditions, maturity, and other factors. If the security is held in the portfolio, its presence in the portfolio will be monitored and credit analysis shall be performed and reported monthly to the Board of Directors.

**ALLOWABLE INVESTMENT INSTRUMENTS PER STATE GOVERNMENT CODE APPLICABLE TO ALL LOCAL AGENCIES**

<b>Authorized Investment</b>	<b>Govt. Code</b>	<b>Maximum Percentage</b>	<b>Maximum Maturity</b>	<b>Minimum Quality</b>	<b>Other</b>
U.S. Treasury Obligations	53601(b)	No Limit	5 Years	None	Notes, bonds, bills, or certificates
U.S. Agency Obligations	53601(f)	No Limit	5 Years	None	Federal agency or U.S. government-sponsored enterprise obligations, participations, or other instruments
EMWD Obligations	53601(a) and (e)	25%	5 Years	None	Bonds or certificate of participation (COP)
California Local Agency Obligations	53601(e)	25%	5 Years	A	Bonds, notes, warrants, or other evidences of indebtedness of a local agency within this state
Supranationals	53601(q)	30% of portfolio & 10% of single issuer	5 Years	AAA	U.S. dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by: <ul style="list-style-type: none"> <li>• International Bank for Reconstruction and Development</li> <li>• International Finance Corporation</li> <li>• Inter-American Development Bank</li> </ul>
Medium Term Notes	53601(k)	30% of portfolio & 5% of single issuer	5 Years	A	Limited to corporations organized and operating within the U.S. or by depository institutions licensed by the U.S. or any state and operating in the U.S.
Bankers' Acceptances	53601(g)	40% of portfolio & 30% of single issuer	180 days	A	Bills of exchange or time drafts
Negotiable Certificates of Deposit	53601(i)	30% of portfolio & 25% of single issuer	1 year	A	<ul style="list-style-type: none"> <li>• Issued by nationally or state-chartered bank, state or federal savings and loan association or by a state-licensed branch of a foreign bank.</li> <li>• Investment shall not exceed the shareholders' equity of depository bank.</li> <li>• Investment shall not exceed the total of the net worth of any depository savings and loan association.</li> </ul>
Commercial Paper	53601(h)	25% of portfolio & 5% of single issuer	270 days	A	Entity shall be organized and operating in the U.S. as a general corporation with total assets in excess of \$500 million and have debt other than commercial paper, if any, that is rated "A" or higher
Local Agency Investment Fund	16429.1 et seq.	As permitted by LAIF	N/A	N/A	Deposits may be made up to maximum permitted by State Treasury policy
County Pooled Investment Funds	53684	15%	N/A	None	Subject to investigation and due diligence as outline in Investment Pools (Section 9)



Authorized Investment	Govt. Code	Maximum Percentage	Maximum Maturity	Minimum Quality	Other
Pledged Funds	53601(m)	No Limit	N/A	None	<p>Invested in accordance with the statutory provisions governing the issuance of those bonds and the ordinance, resolution, indenture or agreement executed by the District, whichever is more conservative.</p> <ul style="list-style-type: none"> <li>• Guaranteed Investment Contract;</li> <li>• Forward delivery agreements collateralized with US Treasury or agencies;</li> <li>• Other investment contracts collateralized with US Treasury or agency securities</li> </ul>
Money Market Funds	53601(l)	15% of portfolio	N/A	AAA	<ul style="list-style-type: none"> <li>• Retain an investment adviser registered or exempt from registration with the SEC with</li> <li>• 5 years' experience managing money market funds in excess of \$500 million; and</li> <li>• Fund must have the highest ranking by not less than 2 NRSRO's</li> </ul>
Mutual Funds	53601(l)	15% of portfolio & 5% from single mutual fund company	N/A	AAA	<ul style="list-style-type: none"> <li>• Fund must invest in securities that comply with the investment restrictions of 53601 (a) through (k) and (n) through (o);</li> <li>• Retain an investment adviser registered or exempt from registration with the SEC with 5 years' experience managing money market funds in excess of \$500 million; and</li> <li>• Fund must have the highest ranking by not less than 2 NRSRO's.</li> </ul>
Joint Powers Authority Pool	53601(p)	15%	N/A	None	
Other: JPA must be organized pursuant to Section 6509.7 that invests in securities in 53601 subdivisions (a) to (q), inclusive and retain investment advisor registered or exempt from registration with the SEC with at least 5 years' experience, and has assets under management in excess of \$500 million.					
Federally Insured Time Deposits		30%	1 Year	None	See below
Other: financial institution must have been in existence for at least 5 years; maintain rating equivalent to an "A" or better from at least one NRSRO; Deposit shall not exceed shareholders' equity of the depository bank; deposit shall not exceed the shareholders' total net worth of depository savings and loan association, unless insured or secured as required by law; the financial institution shall maintain in the collateral pool, securities having a market value of at least 10 percent in excess of the total amount deposited; and promissory notes secured by real estate mortgages or deeds of trust may not be accepted as collateral					
Bond Proceeds		No Limit	N/A	None	Governed by the "Permitted Investments" designated with the respective bond documents for each issuance and statutory law, whichever is most conservative

## 10. PROHIBITED INVESTMENTS

Prohibited investments include inverse floaters, range notes, interest only strips derived from a pool of mortgages, and any security that could result in zero interest accrual if held to maturity. Zero interest accrual means the security has the potential to realize zero earnings depending upon the structure of the security. Zero coupon bonds and similar investments that start at a level below the face value are legal because their value does increase.

## 11. INVESTMENT POOLS

Investigation and due diligence must be completed prior to investing in an investment pool and on a periodic basis thereafter but no more than three years. Investment pools include LAIF (Local Agency Investment Fund), county pooled investment funds, shares of beneficial interest (mutual funds and money market funds), and joint powers authority pools. The investigation will include:

- A description of eligible investment securities, and a written statement of investment policy and objectives.
- A description of interest calculations and how it is distributed, and how gains and losses are treated.
- A description of how the securities are safeguarded (including the settlement process), how often the securities are priced, and how often the program is audited for compliance.
- A description of who may invest in the program, how often, and what size deposit and withdrawal are allowed.
- A schedule for receiving statements and portfolio listings.
- An understanding on if reserves, retained earnings, etc. are utilized by the pool/fund.
- A fee schedule to include when and how it is assessed.
- If the pool/fund is eligible for bond proceeds and/or if it will accept such proceeds.

## 12. COLLATERALIZATION

Certificates of Deposit (CDs) - The District shall require any commercial bank or savings and loan association to deposit eligible securities with an agency of a depository approved by the State Banking Department to secure any uninsured portion of a Non-Negotiable Certificate of Deposit. The value of eligible securities as defined pursuant to California Government Code, Section 53651, pledged against a Certificate of Deposit shall be equal to 150% of the face value of the CD if the securities are classified as mortgages and 110% of the face value of the CD for all other classes of security.

Bank Deposits - This is the process by which a bank or financial institution pledges securities, or other deposits for the purpose of securing repayment of deposited funds. The District shall require any bank or financial institution to comply with the

collateralization criteria defined in California Government Code, Section 53651.

Repurchase Agreements - The District requires that Repurchase Agreements be collateralized only by securities authorized in accordance with California Government Code:

- The securities which collateralize the repurchase agreement shall be priced at Market Value, including any Accrued Interest plus a margin. The Market Value of the securities that underlie a repurchase agreement shall be valued at 102% or greater of the funds borrowed against those securities.
- Financial institutions shall mark the value of the collateral to market at least monthly and increase or decrease the collateral to satisfy the ratio requirement described above.
- The District shall receive monthly statements of collateral.

### **13. DELIVERY, SAFEKEEPING, AND CUSTODY**

Delivery – versus – Payment (DVP) - All investment transactions shall be conducted on a delivery-versus-payment basis.

Safekeeping and Custody - To protect against potential losses due to failure of individual securities dealers, and to enhance access to securities, interest payments and maturity proceeds, all cash and securities in the District's portfolio shall be held in safekeeping in the District's name by a third-party custodian, acting as agent for the District under the terms of a custody agreement executed by the bank and the District. All investment transactions will require a safekeeping receipt or acknowledgment generated from the trade. A monthly report will be received by the District from the custodian listing all securities held in safekeeping with current market data and other information.

The only exceptions to the foregoing shall be depository accounts and securities purchases made with: (i) local government investment pools; (ii) time certificates of deposit, and, (iii) money mutual funds, since the purchased securities are not deliverable.

### **14. PERFORMANCE STANDARDS**

Following the investment policy's statement of objectives, after safety and liquidity of the portfolio are met, the investment portfolio shall be designed with the objective of earning a rate of return throughout budgetary and economic cycles, consistent to the investment risk constraints and cash flow needs of the District. To determine whether market yields are being achieved, the Treasurer shall identify a comparable benchmark in which to compare the District's portfolio. This benchmark is subject to change at the Treasurer's discretion based on changes in market conditions and cash flow requirements.

## 15. REPORTING

The Treasurer shall prepare a monthly report for the Board within 45 days following the end of the month covered by the report and it shall be presented at the next public Board of Directors meeting. The report shall include investment activity, including type of investment, issuer, date of maturity, par and dollar amounts invested on all securities, market value, investments held by local agencies, yield and earnings, and the status of cash by depository.

This report may be made on a quarterly basis but will be at the discretion of the Treasurer. Said report will be included in the agenda as a "Receive and File" document at the Board meeting following submission to the Board Secretary.

## 16. MONITORING SAFETY AND LIQUIDITY OF DISTRICT FUNDS

The Treasurer shall monitor or cause to be monitored the extent to which financial institutions with which District maintains deposits or investments are consistent with District's policies regarding business activities within countries that may jeopardize the safety and liquidity of District funds or violate other District policies. Such matters shall be reported to the Board Administrative Committee as part of the Treasurer's monthly report.

## 17. ADMINISTRATION

The Treasurer may, at any time, further restrict the securities approved for investment as deemed appropriate.

The following officers may open accounts with and deposit and withdraw District funds, to sign checks, drafts, counter checks or orders associated with each of the below listed bank accounts and/or utilize any of the finance approved financial institutions approved by the Treasurer for the purchase and sale of investments, in accordance with the District's Investment Policy. Such activities shall require the approval of one "Primary Signature" and one "Secondary Signature."

### Primary Signature

- President of the Board of Directors
- OR General Manager
- OR Deputy General Manager/(s)
- OR Assistant General Manager/(s)

### Secondary Signature

- Controller
- OR Assistant Chief Financial Officer
- OR Senior Financial Manager
- OR Financial Manager
- OR Board Secretary

## **18. INVESTMENT POLICY REVIEW AND ADOPTION**

The District's investment policy shall be reviewed annually by the Treasurer to ensure it is aligned with the District's strategic priorities and objectives and to ensure compliance with California Government Code.

The District's investment policy shall be adopted by resolution of the Board of Directors. The policy shall be affirmed annually by the Board of Directors.

## **19. GLOSSARY**

**AGENCIES:** Federal agency securities and/or Government Sponsored Enterprises (GSE) which include Federal Home Loan Bank (FHLB), Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), and Federal Farm Credit Bank (FFCB).

**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.

**BOND:** Interest-bearing security issued by a corporation, government, government sponsored enterprise, which can be executed through a bank or trust company. The issuer covenants through an indenture or offering memorandum to pay to the bond holder periodic interest payments and principal at maturity. The bond may be secured by specific assets of the issuer or the general credit of the issuer.

**BROKER-DEALER:** Individual or firm which acts as a principal in security transactions. The District only conducts transactions with approved broker-dealers who meet the requirements of the investment policy.

**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.

**COMMERCIAL PAPER:** Short term, unsecured, negotiable promissory notes issued by domestic corporations.

**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.

**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.

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

**DURATION:** A measure of the sensitivity of the price (the value of principal) of a fixed-income investment to a change in interest rates. Duration is expressed as a number of years. Rising interest rates mean falling bond prices, while declining interest rates mean rising bond prices.

**LIQUIDITY:** A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value. 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.

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

**MEDIUM TERM NOTES:** Corporate and depository institution debt securities with a maximum remaining maturity of five years or less, issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States.

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

**NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATIONS (NRSRO):** A SEC registered agency that assesses the creditworthiness of an entity or specific security. NRSRO typically refers to Standard and Poor's Rating Service, Fitch, Inc. or Moody's Investors Services.

**PORTFOLIO:** Collection of securities held by an investor.

**PAR VALUE:** The face value of a security expressed as a dollar amount. This is the amount due at maturity.

**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-dealers, banks, and a few unregulated firms.

**PRINCIPAL:** The face or par value of a security that does not include interest.

**PRUDENT INVESTOR STANDARD:** 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.

**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 (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.

**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.

**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.

**SUPRANATIONALS:** A supranational organization is formed by a group of countries through an international treaty with specific objectives such as promoting economic development. Supranational organizations also issue debt in the United States. The most commonly recognized supranational debt is the International Bank for Reconstruction and Development (IBRD or World Bank), International Finance Corporation (IFC) and Inter-American Development Bank (IADB).

**TREASURY BILLS:** A noninterest-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.