STATE OF TENNESSEE

TREASURY DEPARTMENT

INTERMEDIATE TERM INVESTMENT FUND

STATEMENT OF INVESTMENT POLICY AS OF FEBRUARY 4, 2013

I. INTRODUCTION

The purpose of this document is to identify various policies and procedures that provide for a prudent and systematic investment process. The initial step toward a prudent investment policy is to organize and formalize investment-related activities. Related activities which comprise good cash management include accurate cash projection, the expeditious collection of revenue, the control of disbursements and cost-effective banking relations.

II. SCOPE

Pursuant to Tenn. Code Ann. §9-4-608, the Intermediate Term Investment Fund ("Fund") is authorized to receive and invest any money in the custody of any department or agency of the state, which is required, by court order, contract, state or federal law or federal regulation to receive interest on invested funds; from any County Trustee that has been authorized by resolution adopted by the county legislative body; or from any other participant in the State Pooled Investment Fund ("SPIF"), notwithstanding Tenn. Code Ann. §5-8-301. This policy covers only funds and investment activities specifically addressed in this statute.

III. OBJECTIVES

A. This portfolio is intended to be a longer-term option for investment of funds as an alternative to the SPIF (which includes the Local Government Investment Pool ("LGIP"). The market value of this portfolio will decline in a period of rising interest rates. Participants will share income, capital gains or losses on a pro rata basis. Due to the longer-term nature of investments in this Fund, it is anticipated that participants will make limited numbers of deposits and withdrawals from the Fund.

B. Investment decisions should not incur unreasonable investment risks in order to obtain current investment income.

C. The Fund portfolio shall be designed to invest funds in longer-term investments than the SPIF in order to benefit from the normal steepness of the yield curve.

D. While the State will not make investments for the purpose of speculating as the dominant criterion, the State Treasurer shall seek to enhance total portfolio return by means of active portfolio management. The prohibition of speculative investments precludes pursuit of gain or profit through unusual risk; however, trading in response to changes in market value or market direction is warranted under active portfolio management.

E. All participants in the investment process shall act responsibly as custodians of the public trust. Investment officials shall recognize that the investment portfolio is subject to public review and evaluation. The overall program shall be designed and managed with a degree of professionalism that is worthy of the public trust.

F. The Fund shall be established when the minimum set forth in Section XVIII is achieved. The minimum amount that each participant can invest shall be fifty thousand dollars ($50,000), and the maximum amount that each participant can invest shall be equal to fifteen percent (15%) of the participant's operating account balance. Bond proceeds, restricted accounts, or other special account funds shall not be subject to the fifteen percent (15%) limit.

IV. DELEGATION OF AUTHORITY

The responsibility for administering the Fund resides with the State Treasurer pursuant to Tenn. Code Ann. §9-4-608 and shall be exercised in accordance with this investment policy and resolutions of the State Funding Board ("Board"). Responsibility for day-to-day administration of this policy may be assigned by the State Treasurer to appropriate investment officials within the Treasury Department.

V. CORRECTIVE ACTION

The Treasurer may take such corrective actions, including but not limited to the following, that the Treasurer determines in his discretion are in the best interests of the participants in the Fund, are necessary and appropriate in consideration of market conditions or other factors (including, but not limited to regulatory or accounting requirements), subject to and in compliance with applicable laws and rules:

1. restricting or suspend the sale and redemption of Shares, in such amounts and upon such time restrictions as the Treasurer deems necessary and appropriate;
2. selling securities in the Fund prior to maturity to realize capital gains or losses or to shorten average Fund maturity;
3. withholding earnings otherwise payable to participants;
4. making special capital distributions;
5. redeeming Shares in kind;
6. establishing a net asset value per share by using available market quotations;
7 increasing, reducing, suspending or deferring the imposition of the fee to administer the Fund; or
8. terminating the Fund.

Such actions and the reasons therefor shall be reported to the Board and participants in the Fund to their last known email addresses of record and shall also be posted to the website of the State Treasurer as soon as reasonably possible.

VI. REPORTING

Quarterly

The State Treasurer shall submit a quarterly investment report to the Board; the Speaker of the House of Representatives; the Speaker of the Senate; the Chairmen of the Finance, Ways and Means Committees of the House and Senate; and the Chairman of the Fiscal Review Committee. This report will describe the portfolio activity during the period and compute the average yield and average maturity of the portfolio. The report shall summarize the investment strategies employed in the most recent period and shall also describe the investment portfolio in terms of investment securities; maturities; investment return compared to budgetary expectations; yield; and average maturity of the total portfolio. Each report shall indicate any areas of policy concern and suggested or planned revision of investment strategies.

Annual

Annually, the State Treasurer shall present a comprehensive annual report on the investment program and investment activity to the Board; the Speaker of the House of Representatives; the Speaker of the Senate; the Chairmen of the Finance, Ways and Means Committees of the House and Senate; and the Chairman of the Fiscal Review Committee. This report shall include twelve (12)-month comparisons of return, shall suggest policies and improvements that might enhance the investment program, and include an investment plan for the ensuing fiscal year.

VII. AUTHORIZED INVESTMENT INSTRUMENTS

Pursuant to Tenn. Code Ann. §9-4-602, the following are the permitted investment instruments for purchase by the Fund:

A. Bonds, notes, and treasury bills of the United States or other obligations guaranteed as to principal and interest by the United States or any of its agencies.

B. Obligations guaranteed as to principal and interest by the federal home loan mortgage corporation, federal national mortgage association, student loan marketing association and other United States government-sponsored corporations.

C. Repurchase agreements for obligations of the United States or its agencies.

D. Prime commercial paper that is rated in the highest category by at least two (2) nationally recognized commercial paper rating services.

E. Prime bankers' acceptances that are eligible for purchase by the Federal Reserve System.

VIII. INVESTMENT TERMS AND CONDITIONS

A. The following terms and conditions shall apply to investment in United States government or agency securities:

1. The maximum time period from date of acquisition to maturity of government or agency securities may not exceed five (5) years.

2. The Board does not deem it necessary to leverage or hedge the Fund and, therefore, use of derivative type securities is inappropriate. Only securities of the type enumerated in this policy may be acquired. Accordingly, securities such as the following are prohibited investments: futures, contractual swaps, options, exotic derivatives (e.g., range notes, dual index notes, and inverse floating rate notes), and no equity investments of any type.

B. The following terms and conditions shall apply to investment in commercial paper:

1. Prime commercial paper, including asset-backed commercial paper, which shall not have a maturity that exceeds two hundred seventy (270) days.

2. Acquisitions will be monitored to assure that no more than five percent (5%) of the portfolio market value at the date of acquisition shall be invested in prime commercial paper of a single issuing corporation. The total holdings of an issuer's paper should not represent more than five percent (5%) of the issuing corporation's total outstanding commercial paper.

3. Purchases of prime commercial paper shall not exceed thirty-five percent (35%) of the Fund's market value at the date of acquisition.

4. Purchases must be limited to corporations that meet the criteria for investment by the SPIF.

5. Issues may be acquired from authorized broker/dealers or directly from an eligible issuer.

C. The following terms and conditions shall apply to investment in the use of repurchase agreements:

1. Securities purchased under the repurchase agreement shall be limited to the securities and qualifications listed in Section VI., Item A and Item B.

2. Securities shall be marked-to-market daily and shall be maintained at a value equal to or greater than the cash investment.

3. At the time of purchase, the market value of the securities shall be one hundred and two percent (102%) of the cash investment.

4. All securities purchased under a repurchase agreement shall be held by a third party custodian.

5. The seller of repurchase securities shall be entitled to substitute securities, only by prior authorization from authorized personnel of the Treasury Department. New or substitute securities should be reasonably identical to the original securities in term of maturity, yield, quality, and liquidity. Investments in repurchase agreements shall be generally used to maintain a liquidity margin and to ensure that funds are fully invested to the maximum extent practical. Due to varied liquidity requirements, the amount invested in repurchases is not limited. Repurchase agreements shall not be used as a primary investment vehicle. Individual repurchase agreement transactions shall not have a maturity that exceeds ninety (90) days. Only broker/dealers and state depositories that complete the appropriate State's master repurchase agreement will be considered for repurchase transactions.

D. The following terms and conditions shall apply to investment in banker's acceptances:

1. Prime banker's acceptances must be issued by domestic banks with a minimum AA long term debt rating or foreign banks with an AAA long term debt rating by a majority of the designated rating services that have rated the issuer. The short-term debt rating must be at least A1 or equivalent by all of the rating services that rate the issuer (minimum of two ratings must be available).

2. Prime banker's acceptances shall not exceed five percent (5%) of the Fund's book value on the date of acquisition. The amount invested in any one commercial bank pursuant to this paragraph cannot exceed five percent (5%) of the book value of the portfolio on the date of acquisition or twenty-five million dollars ($25,000,000), whichever is less.

   a. Prime banker's acceptances must be eligible for purchase by the Federal Reserve System as required by Tenn. Code Ann. §9-4-602(a)(1)(B)(i)*(f)*. A prime banker's acceptance must have an original maturity of not more than two hundred seventy (270) days to be eligible for purchase and it must:

      (1) Arise out of the current shipment of goods between countries or within the United States; or

      (2) Arise out of storage within the United States of goods under contract of sale or expected to move into the channel of trade within a reasonable time and that are secured throughout their life by a warehouse receipt or similar document conveying title to the underlying goods.

3. It is the policy to buy prime banker's acceptances to hold to maturity. Banker's acceptances may be traded in the secondary market to maintain liquidity. The Cash Management Division will report any banker's acceptances sold prior to maturity to the Treasurer.

E. The following policy will apply to acquisitions or sale of securities other than commercial paper or repurchase agreements:

1. Securities shall be purchased through authorized broker/dealers for the security to be acquired;

2. All transactions will be executed on a delivery versus payment basis. Due bills or notes are not acceptable as collateral in lieu of the purchased security; and

3. All transactions will be traded in U. S. dollars.

IX. PRUDENCE

The standard of prudence to be used by investment staff shall be the "prudent person rule," which obligates a fiduciary to ensure that:

> ". . . investments shall be made with the exercise of that degree of 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."

The Treasury Department's investment staff shall disclose to the State Treasurer the following information regarding family members that are employed by a broker/dealer or other entity in which State funds might be invested or in which investment transactions might be processed: family member's name and relationship to employee, their title/position with the company and the nature of transactions that might be made between the State and that company. Investment staff shall also disclose to the State Treasurer any intentions of investing personal funds or funds for others with any broker/dealer authorized to transact business for the State before such transactions are completed.

X. INTERNAL CONTROLS

The State Treasurer shall establish a system of internal controls, which shall be documented in writing. The controls shall be designed to prevent losses of public funds arising from fraud, employee error, misrepresentation by third parties, unanticipated changes in financial markets, or imprudent actions by employees and officers of the State. Controls deemed most important include: control of collusion; separation of duties; separating transaction authority from accounting and recordkeeping; custodial safekeeping; clear delegation of authority; minimizing the number of authorized investment officials; documentation of transaction strategies; and code of ethics.

XI. BROKER/DEALER SELECTION AND REVIEW

The list of approved broker/dealers used by the SPIF will be used for this Fund.

XII. MATURITY

The dollar weighted average maturity of the Fund shall not exceed three (3) years. An appropriate amount of the Fund will be maintained in short term investments to cover emergency withdrawals. No security will be bought with a remaining life of over five (5) years.

XIII. CASH MANAGEMENT

In order to efficiently administer the Fund, the State's SPIF may be used for the purposes of cash administration, but shall not be used for the purposes of investment.

XIV. DIVERSIFICATION

It is the State's policy to diversify the investment portfolio in order to reduce the risk of loss resulting from over-concentration of assets in a specific maturity, a specific issuer, or a specific class of securities.

XV. RISK TOLERANCE

The State 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 way to control risk. Investment managers are expected to display prudence in the selection of securities, as a way to minimize default risk. No individual investment transaction shall be undertaken which jeopardizes the total capital position of the overall portfolio. Securities may be sold at a loss if required to meet current expenditures or if involved in portfolio management decisions pursuant to section III. D. of this policy statement.

XVI. SAFEKEEPING AND CUSTODY

All securities purchased shall be held by a custodian pursuant to a custodian agreement. To protect against potential fraud and embezzlement, other assets of the State shall be held in the State's vault or secured through third-party custody and safekeeping procedures. Safekeeping procedures shall be reviewed annually by the internal auditor. The internal auditor may conduct unscheduled audits of safekeeping and custodial procedures.

Securities that are actively traded in a secondary market should be priced by an independent pricing service. Prices provided by an independent pricing service should be updated to the investment accounting portfolio system daily, if possible. Commercial paper, bank deposits, and repurchase agreements do not actively trade in a secondary market and will be carried at amortized cost..

XVII. DEPOSIT AND REDEMPTION RESTRICTIONS

Participants in the Fund are advised to only invest monies in this fund that are not needed for short term liquidity because the daily value of the fund will be priced to market and could have significant price volatility. If participants redeem shares (withdraw funds) when the market is depressed they will incur losses that would not likely occur if sufficient funds were held for liquidity in the SPIF or other similar short-term investments. The Fund will not maintain a significant position in cash equivalent investments. As a result, a participant who desires to redeem shares (withdraw funds) may not be able to receive funds until sufficient liquidity is achieved by the Fund.

Purchases and redemptions can only be made on the first working day of each quarter. Thirty (30) days notice is required for redemptions. If the State Treasurer determines that an urgent need exists, the thirty (30) day notice may be waived. The State Treasurer may limit or suspend the purchase or redemption of shares with notice of such action and the reasons therefore communicated to the Board and participants as soon as reasonably possible.

A participant in the Fund may not be able to redeem its shares in the fund at the same value at which the shares were purchased. The State of Tennessee, the FDIC, nor any other state or federal agency does not guarantee that a participant will receive the value of its investment or interest thereon upon redemption of its shares.

XVIII. APPROVAL REQUIRED

A participant must be approved by the State Treasurer to participate in the Fund before any participant may purchase shares of the Fund.

XIX. MINIMUM REQUIREMENT TO IMPLEMENT THE INTERMEDIATE TERM FUND

In order to establish an efficient and diversified Fund, the State Treasurer must receive a total of at least $50,000,000 from eligible participants.

XX. TERMINATION OF FUND

If the Board determines that the Fund will be terminated, the Treasurer shall issue a written notice within sixty (60) days from the Board's determination to terminate, with notice of such termination communicated to the Fund's participants and the Board to their last known email addresses of record, and posted to the website of the State Treasurer as soon as reasonably possible. The Treasurer may terminate the Fund immediately, pursuant to Section V herein, with notice of such termination communicated to the Fund's participants and the Board, to their last known email addresses of record, and posted to the website of the State Treasurer as soon as reasonably possible.

XXI. ADMINISTRATIVE FEE

The Treasurer shall establish a revolving account that is under the Treasurer's custody in order to defray the administrative costs associated with the Fund. The Treasurer shall deduct a reasonable charge for administering the Fund from each Participant's pro rata earnings through the Fund which sum shall be deposited and expended through the revolving account; however, the Treasurer may increase, reduce, suspend or defer the imposition of the fee to administer the Fund when he determines that it is necessary and appropriate.

XXII. INVESTMENT POLICY ADOPTION

This investment policy is adopted by the Board pursuant to T.C.A 9-4-608, as attested below, and may only be changed by subsequent action of the Board.

Attest:

State Funding Board Secretary

2/4/13

Date