Commonwealth of Puerto Rico
AUTOMOBILE ACCIDENTS COMPENSATIONS ADMINISTRATION

STATEMENT OF INVESTMENT POLICY, OBJECTIVES AND GUIDELINES

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STATEMENT OF INVESTMENT POLICY, OBJECTIVES AND GUIDELINES

I. Definitions

A. AACA

The Automobile Accidents Compensations Administration (ACAA for its acronym in Spanish) is a public corporation of the Commonwealth of Puerto Rico created by Act 138, enacted June 26, 1968, also known as the Automobile Accidents Social Protection Act, which provides for compensations for the victims of traffic accidents, thus fulfilling its mission of reducing the tragic socioeconomic effects that the traffic accidents bring upon the families and other dependents of the aforementioned victims. ACAA is exempted from Puerto Rico and U.S. taxation.

The general responsibility and effective operation of the Administration rests on its Board of Directors, as provided by the Law.

B. The Board of Directors

The Corporate powers of the Administration are exercised by a Board of Directors that is also responsible for the administration and assuring the enforcement of the dispositions of this Law.

The Board is composed by one member of the Cabinet and four additional Directors appointed by the Governor with the advice and consent of the Senate. At least two of the four Directors represent the public interest and one is a person experienced in the insurance business. Three Directors of the Board shall constitute quorum. The Board has a President and a Secretary.

C. Executive Director

The Board appoints an Executive Director who is responsible for the direct administration of the corporation according to the laws, standards and conditions that the Board may establish.

D. The Investment Fund

The Investment Fund (the Fund) is that portion of the Fund investment portfolio, which includes ACAA's assets (stocks, bonds, real estate and cash equivalents).

E. The Investment Consultant

The Investment Consultant (the Consultant) shall be a professionally qualified company which has the necessary specialized research facilities and skilled personnel to provide objective, impartial. investment management counseling. The Board, through its Executive Director, shall engage the Investment Consultant.

F. The Investment Manager

The Investment Manager(s) (the Manager(s), shall be one or more professionally qualified companies which has the necessary specialized research facilities and skilled personnel to provide objective, impartial investment advice and discretionary investment management of securities portfolios on a continuous basis. The Manager(s) shall be registered investment advisor under the Investment Advisors Act of 1940 and duly registered with the Securities & Exchange Commission. The Board through its Executive Director shall engage the Manager(s).

G. The Master/Custodian

The Master/Custodian Bank shall be a professionally qualified institution, with the necessary specialized facilities and skilled personnel to provide accurate and timely safekeeping of the assets of the Fund.

II. <u>Purpose of the Investment Policy Statement</u>

A. This Statement of Investment Objectives and Policy Guidelines is set forth in order that:

1. The Board, the Consultant and the Manager(s) have a clear and joint understanding of the investment objectives and policies of ACAA's Investment Fund,

2. The Manager(s) is given guidance and limitations in investing the funds of ACAA, and

3. The Board and the Consultant have a meaningful basis for the evaluation of the performance of the Manager(s) to meet the fiduciary duty to prudently monitor the investments of the Fund.

B. The investment objectives and policy guidelines that follow represent the current consensus of the Board's philosophy regarding the investment of the Fund assets. This Statement will be reviewed and possibly revised from time to time to ensure that it continues to reflect the Board's attitude, expectations and objectives. All modifications or amendments of the investment policies shall be in writing. The Manager(s) and the Consultant are encouraged and expected to provide constructive feedback and suggestions to the Board regarding the investment objectives and policy guidelines.

C. It is the intent of this document to state general attitudes, guidelines and philosophy that will guide the Manager(s) toward the performance desired. It is intended that the investment policies be sufficiently specific to be meaningful, but adequately flexible to be practicable.

III. Responsibilities of the Board of Directors

A. With respect to the investments of the Fund, the specific responsibilities of the Board in the investment process include the following:

1. To establish reasonable investment objectives,

2. To develop sound and consistent investment policy guidelines, which the Manager(s) must use in formulating corresponding investment decisions,

3. To express the Fund's risk tolerance,

4. To evaluate and select a qualified Manager(s), qualified Investment Consultants and qualified Master Custodians,

5. To consider, if appropriate and necessary, the inclusion in the evaluation process of investment managers that qualify under the Minorities Opportunity Act. However, the Investment Manager will be evaluated under the same performance criteria as applied to any other investment manager,

6. To determine and monitor the appropriate portfolio construction and allocation of assets to various investment categories,

7. To review the investment objectives and guidelines at least once a year, so as to respond to changing conditions which may develop from time to time,
8. To take appropriate action to replace the Consultant and/or the Manager(s) for failure to perform as expected,

9. To monitor and evaluate performance results to assure that objectives are being met,

10. To assure that the investment program is in compliance with all applicable laws and regulations of the Commonwealth of Puerto Rico, and

11. To assure that the investments of the Fund are administered at a reasonable cost, being careful to avoid sacrificing quality. These costs include, but are not limited to, management and custodial fees, consulting fees, transaction costs and other administrative costs chargeable to the Fund.

B. The Board recognizes that its role is supervisory, not advisory, and that determination of investment strategy and securities selection shall be delegated to the Manager(s), according to policies stated herein.

IV. Responsibilities of the Investment Consultant

A. Regarding to the investments of the Fund, the Consultant is charged with the responsibility of facilitating the following processes:

1. Assuring a clear understanding by all parties of:

    a. the financial objectives of ACAA, for its portfolio investment,

    b. a basic understanding of the fiduciary duties of the Board and the Manager(s), and

    c. practical comprehension of the capital markets, such that investment decisions reflect sound management of the Fund.

2. The on-going **review of ACAA's Statement of Investment Policy Guidelines and Objectives**, to insure that it adequately reflects the investment philosophy, strategies, objectives and guidelines subscribed to by the Board.

3. The on-going **examination of ACAA's investment portfolios**, to insure:

    a. complete compliance with the Fund's investment policy guidelines. Such compliance must be exercised through on-going examination of each of the assets held in the investment portfolio, to assure that the asset allocation; quality, maturity and other guidelines stated herein are so honored. Any violation of guidelines will be communicated verbally and in writing to the Manager(s), to the Board and to the Administration.

  b. the attainment of the Fund's investment objectives over market cycles (3-5 years).

4. On-going **due diligence of the Manager(s)**, in order to insure:

  a. Adherence to the investment style for which the Manager(s) was hired, and

  b. that the quality of the investment management firm remains high, relative to its investment style, peer group, infrastructure and performance.

5. The on-going **performance measurement of the investment process**, in order to insure:

  a. that performance obtained contributes positively and adequately to the overall performance of the Fund, relative to investment style, peer group and the Fund's investment objectives. **Such performance shall be computed according to the standards set forth by the Association of Investment Management and Research.**

6. The on-going **transaction cost analysis** to insure that the Fund is provided with the best execution possible on all transactions.

7. The on-going **communication with the custodian** to insure that the Fund receives:

  a. detailed confirmations on all transactions,

  b. detailed and accurate monthly statements and daily on-line access to the information, which reflect all transactions, additions, withdrawals and deposits for the month.

B. The Consultant will provide a quarterly monitor to ACAA, which will incorporate or take into account all investment activity for the quarter:

1. Purchases and sales
2. Deposits and withdrawals
3. Dividends and interest credited
4. Realized capital gains and losses

5. Statement of assets

C. The Consultant will provide quarterly performance measurement reports, which will gauge the changes in asset value of the Fund and display these changes versus stated objectives, as well as **hybrid indices**, which conform to the specific asset allocation parameters of the Fund.

D. The Consultant shall promptly inform, orally and in writing, to the Board and the Executive Director of any investment practice which, has fallen outside of this Policy. The Administration will then take such action, as it deems necessary and prudent.

E. To recommend adjustment or changes to the investment Policy when considering it necessary.

F. Full compliance of all the terms and conditions of the consultant contract.

V. Responsibilities of the Investment Manager(s)

A. Eligibility

The Board agrees that the Manager(s) must meet the following general **criteria for eligibility**:

1. The Manager(s) must be duly registered with the Securities and Exchange Commission as an investment advisor under the Investment Advisors Act of 1940, or duly registered as a bank or trust company under Puerto Rico or US law and/or duly registered with the Commissioner of Financial Institutions of Puerto Rico.

2. The Manager(s) must be a substantial, financially viable organization with superior equity **and/or** fixed income security management, capable of supporting an investment process and delivering consistently superior returns. This evaluation may include, but is not limited to, producing superior risk-adjusted performance relative to the capital markets, the Manager(s)' peer group and to a benchmark that reflects the Manager(s) investment style, for ten (10) years or five (5) years, as well as the trailing twelve (12) month period. Other different rolling time periods may be included in the analysis in an effort to analyze the Manager's performance consistency.
3. The Manager(s) must have a clearly defined organizational structure with staffing, facilities and operations capable of

supporting the investment activities and servicing requirements of the Fund.

4. The Manager(s)' investment professionals should have extensive practical experience in the field of investment management.

5. The Manager(s) is expected to acknowledge in writing its recognition and acceptance of full responsibility as a fiduciary under applicable federal and local legislation.

6. Funds placed with the Manager(s) should not constitute more than **10%** of total assets under the Manager(s)' management.

7. The Manager(s) should be able to articulate a clearly defined investment process: i.e., a buy and sell discipline with its overall investment strategy.

8. The total quantity of accounts managed by each "portfolio manager" will be of consideration.

B. Responsibilities

The Manager(s) hired by the Board will be charged with the following on-going responsibilities:

1. Performance

a. To determine and implement investment strategy and securities selection, within the guidelines stated herein.

b. To assure that the Fund under the Manager(s)' management performs as well or better than the Manager(s)' equity and fixed income components, translated to a composite as set forth herein.

c. To assure that the nominal investment objectives of the Fund are met, while adhering to the policies and guidelines stated herein.

d. To steadfastly maintain the investment style and portfolio characteristics that were professed at the time of engagement.

e. To conduct all security trading transactions on a "best execution" basis. The Investment Manager shall not execute any transactions through its own company or any affiliate or

related brokerage firm, if such a relation exists.

f. To assure that transactions are executed and settled avoiding cash overdraft.

g. To vote the proxies in the spirit and context of the guidelines and restrictions governing the Fund's investments.

h. Investment Managers must reconcile with the Custodian at least on a quarterly basis. Such reconciliation must be provided to ACAA along with an explanation of any discrepancies and how they will be resolved.

2. Communication

a. **To assure that the portfolio manager is directly responsible for managing the Fund, he should meet at least once a year** with the Board, as well as at such other times as requested by the Board, in order to provide the following:

1) Review the past, present and prospective economic climate in relation to investment strategy.

2) Allow the Board to understand the investment strategy being used to fulfill the stated objectives.
3) Allow the Board to understand the risk levels of the securities represented in the portfolios.

4) Review and evaluate trends in performance levels in relation to stated objectives.

5) That the Board has the opportunity to advise the Manager(s)' of any significant changes in investment policy.

6) Allow the Board to meet the key person in charge of the account.

b. To inform the Board, within 24 hours, if any of the following events occur:

1) Any changes in the management or ownership of the investment management firm
2) Any loss of key investment personnel

3) A change in the investment philosophy that represents a deviation from this policy

4) Any situation that has the potential to impact either the professionalism, financial position or integrity of either the Manager (s) firm, or the Fund;

5) A loss of a key investment client. A key investment client is defined as an account that represents 10% or more of the total assets managed by the money management firm.

c. To inform the Board of any changes in the quality ratings of securities in the Fund, which may cause said securities to fall below the quality standards stated herein. Such communication will be immediate, oral and in writing to the Board and the Executive Director.

d. To make sure that confirmations of all transactions are sent to ACAA.

3. Agreements

The Manager(s) will enter into a written Investment Management Agreement with ACAA, in which fees and other related matters will be set forth. In that Agreement, the Manager(s) will acknowledge receipt of and intent to comply with the policies and guidelines stated herein.

C. On-going Evaluation

1. The Investment Manager(s) shall **at all times** maintains the qualitative and performance standards stated in Sections V A and V B above.

2. The Consultant will measure the Manager(s)' adherence to this investment policy throughout the term of his/her contract. Any deviation may be grounds for replacing the Manager(s).

3. While the Board intends to fairly evaluate the portfolio's performance during 3-5 years periods and other relevant time periods, it reserves the right to replace the Manager(s) at any time. The most serious threat to the Board's confidence regarding any Manager is breach of the Fund's risk tolerance (as defined in Section IX B) and investment guidelines.

4. For more detail on the guidelines that may be used to try to monitor the performance of the money managers, please see Section X, Review Meetings and Communications, Subsection B, *Guidelines Related to the On-going Monitoring of the Money Managers.*

VI. Responsibilities of the Custodian

The Custodian has the following responsibilities:

A. To insure the accurate and timely settlement of all transactions.

B. To insure the accurate and timely crediting of dividends and interest on all securities, and to credit principal paid on called or matured securities of the Fund.

C. To maintain accurate records of all credits, contributions and withdrawals of the Fund.

D. To provide detailed and accurate monthly statements and daily on-line access to the information which reflects all transactions, deposits, contributions and withdrawals for the month.

E. To distribute proxy information and monitor the proxy processing of the Fund holdings.

VII. Statement of Investment Goals and Objectives-General

A. Investment Goals:

1. To maximize, without undue risk, the return from the assets of the Fund.

2. To assure adequate cash flow and liquidity levels so that ACAA may fulfill its obligations on an on-going basis.

B. Investment Objective:

In achieving these goals, the Board primarily seeks consistency of investment return through the investment objective of total return. Total return is defined as the sum of dividends, interest, plus realized and unrealized capital gains, for the given period. Specifically, the Board seeks a minimum total return equivalent to the rate of inflation, as measured by the Consumer Price Index, plus no less than 4%, net of fees and expenses.

The target long-term annual return will be updated periodically based on new long-term asset allocation studies. Each updated asset allocation study shall produce an updated target return for the Fund.

The achievements of these objectives should be obtained so that the Fund is protected from excessive volatility in market value over market cycles (3-5 years). The minimum objective should be achieved over rolling five-year periods on a real total-return basis while the annual target return would be based on a rolling twelve-month period.

The achievement of this objective should be obtained so that the Fund is protected from excessive volatility in market value

C. Benchmarks:

1. **Total return from investments should exceed inflation (as measured by the Consumer Price Index) by no less than 4%, net of fees and expenses.** The level of return is important to the strength of the Fund; it is second only to safety in importance. In order to assure that this objective is met, return will be measured against the following three variables:

   a. The Fund's actuarial return objective

   b. C.P.I. + 4%

   c. the ACAA Index, a hybrid index composed of the Russell 1000 Value Index, the Russell 1000 Growth Index, a combination of the appropriate Russell Mid Cap or Russell Small Cap Indices (according to the Manager hired at any given time), the Morgan Stanley All Country World Index xUnited States, the Barclays Capital Intermediate Government/Corporate, the Salomon Brothers World Government Bond excluding US, hedged to $US dollar Index, the NAREIT Equity Real Estate Index (or the NCREIF Real Estate Index) and the US 90-day Treasury Bill, so weighted as to reflect the preferred asset allocation of the Fund.

2. The performance of each Manager should be measured against each Manager's appropriate benchmark index. Each manager is expected, during a full business cycle, to outperform the corresponding index.

Asset Category	Comparative Index	Peer Group Universe
Equities:		
Large Cap Equity: Value Growth Core	S&P 500 / Russell 1000 S&P 500 Barra Value / Russell 1000 Value S&P 500 Barra Growth / Russell 1000 Growth S&P 500 / Russell 1000	Total Equity Database Value Equity Style Growth Equity Style Core Equity Style
Mid Cap Equity	S & P 400 / Russell 2500 or Rusell MidCap	Mid Cap Equity Style
Small Cap Equity	S & P 600 / Russell 2000	Small Cap Equity Style
International Equity – Developed and Emerging Mkts	Morgan Stanley All Country World Index xUnited States	International Equity Style
Fixed Income:		
Intermediate	BC Intermediate Gov. Credit Bond Index	Intermediate Fixed Income Style
Puerto Rico Bonds	Barclays Aggregate Bond Index or other proxy (no specific index for PR bond exists)	Not Available
Real Estate	NCREIF or NAREIT Equity Indices	Real Estate Database
Cash	90 day T-Bills	Money Market Database

VIII. General Investment Philosophy and Guidelines

A. The Fund shall be managed according to the following covenants:

1. The Investments of the funds of ACAA shall be made solely in the interest of ACAA's goals and objectives and for the exclusive purpose of providing the source of payment of benefits to participants and their beneficiaries and defraying reasonable administrative expenses.
2. The Fund shall be invested with the care, skill, prudence and diligence under the circumstances prevailing from time to time that a prudent person acting in that position and familiar with such matters would use in the investment of a fund of that nature and with such purposes.

3. The investments of the Fund shall be so diversified as to minimize the risk of large losses, unless under particular circumstances it is clearly prudent not to do so.

B. Economy

The Board is sensitive to significant changes in the economy, such as varying short and long-term interest rates and changing rates of inflation.

It will be the responsibility of the Manager(s) to choose and manage investments within the General Guidelines of the Fund that will optimize results on the basis of prevailing economic conditions.

C. Safety of Principal

It is believed that the criterion of safety of principal need not be imposed on each individual investment. However, the portfolio taken as a whole must be structured primarily to protect it against the long-term erosion of capital.

D. Liquidity Requirements

ACAA's Finance Department shall determine ACAA's cash flow requirements for each fiscal year. The Manager(s) will be informed in order that appropriate reserves are made available on a quarterly basis. Reserves shall be deposited at the custodian's Short Term Investment Fund (STIF) until withdrawal.

E. Turnover

It is the responsibility of the Manager(s) to select the turnover needed to achieve the performance objectives. If performance results meet the Fund's investment rate of return objective, the rate of turnover will not be an evaluative factor. **Transactions shall always be undertaken on a *best execution* basis.**

F. Types of Assets

In order to provide the Manager(s) with the freedom to invest in various types of assets, the following types of assets are approved for investment (the Manager(s) shall consult the Risk Management Guidelines of the Fund for details on asset allocation parameters of each type of asset):

1. Common stocks and preferred stocks

2. Convertible bonds and convertible preferred stocks except for Puerto Rico Investments

3. Money market funds and bank-sponsored short-term investment funds

4. Purchase agreements[1]

5. Commercial paper

6. Domestic and US Dollar-denominated Euro Banker's Acceptance

7. Domestic and US Dollar-denominated Euro Time Deposits

8. Domestic and US Dollar-denominated Euro Certificates of Deposits

9. Corporate bonds and notes

10. US Government Treasury Bills, Notes and Bonds

11. United States GNMA's pass-throughs

12. Bonds and notes of US government agencies

13. Mortgage pass-through guaranteed by FNMA or Freddie Mac

14. CMO's collateralized by GNMA's, FNMA's or Freddie Macs and NCUA

15. Obligations of the Commonwealth of Puerto Rico and its instrumentalities

16. Asset-backed fixed income securities

17. Commercial mortgage-backed securities

18. Rule 144A securities are permitted, if these comply with credit quality, liquidity and other relevant considerations specified in this IPS.

19. Investments in real estate, directly or through limited partnerships or other investment vehicles that invest exclusively

[1] The Fund shall engage only in repurchase agreements collaterized by US Government Securities

in real estate.

As part of its fiduciary responsibility, the Board intends to review from time to time the approved types of assets listed above.

G. Prohibited Transactions

The following types of assets or transactions are expressly prohibited:

1. Options contracts - the purchase and sale of put and call options, except for the writing of covered call options for capital preservation purposes[2]

2. Commodities

3. Purchase of equity securities on margin

4. Short selling

5. Interest-only (IO), Principal-only (PO), and CMO residuals

6. Transactions that would leverage investment positions except for securities lending operations.

7. Off-balance-sheet derivates

8. Limited partnerships that invest in assets other than real estate (limited partnerships that are professionally managed and invest exclusively in real estate are the only limited partnerships that ACAA may invest in).

9. Venture capital investments

10.
11. Others that may be specified by the Board in writing from time to time.

12. Investment in companies whose primary source of revenues is related to the alcohol industry as defined by the Standard Industry Code.

13. Non marketable securities

14. Convertible or preferred securities (only in Puerto Rico

[2] It is understood that this item does not include Fixed Income Securities that have a put or call feature.

investments)

15. Reverse repurchase agreements or securities lending (only in Puerto Rico investments)

16. Mutual funds or group trusts unless approved by the Board of Directors of ACAA.

IX. Investment Guidelines on Managing Risk

The Board best describes risk as a high degree of fluctuation in the market value of the portfolio within a market cycle. In order to reasonably control this risk, the Board sets forth the following parameters and guidelines, which are designed to complement the investment principles used by the Board, namely: security, diversification, high return, and marketability.

A. Asset Allocation under Professional Investment Management
The Board has established the following asset allocation parameters for the total portfolio:

	Lower Limit	Strategic Allocation	Upper Limit	Benchmark
U.S. Common Equity	***20%***	***35.5%***	***45%***	
Large Value		14.50%		R1000Value
Large Growth		14.50%		R1000Growth
Mid/Small Cap		6.50%		Russell Mid/Small Cap Blended
International Equity-Developed and Emerging Mkts	***4.00%***	***10.5%***	***15.00%***	Morgan Stanley All Country World Index xUnited States
Domestic Bonds	***3 0%***	***40.0%***	***55%***	BC Intermediate Gov/Credit Bond Index
Intermediate		40.00%		
Municipal Bonds	*0%*	*5.00%*	10%	
Puerto Rico Bonds	***0%***	***4.50%***	***7.00%***	No index of PR bonds available; could use US bonds indices or other proxies, but they are of limited comparison value
Real Estate	***0.00%***	***5.00%***	***7.00%***	***NAREIT Equity Real Estate Index or other RE Index (such as NCREIF RE Index)***
Cash & Equiv.	***0.10%***	***1.00%***	***10.00%***	***90 Day T-Bill***
TOTALS		***100.00%***		

The allocation for each equity investment style (e.g. "Large Value) is intended to be general in nature and is not always expected to be at the specified "Strategic Allocation" target. For risk control purposes (i.e. lower and upper limits), please refer to the stated ranges in the main asset class in bold (e.g. "U.S. Common Equity").

Portfolio assets will be allocated among various investment managers with distinct styles and philosophy. Each of the Managers shall operate under a set of investment guidelines specific to the strategic role its' portfolio is to fulfill in the overall investment structure. **Certain strategies followed by specific Managers may require special instructions given through a *side-letter* from the Executive Director to the Manager with the approval of the Board of Directors.**

B. Risk Management Guidelines

1. Total Portfolio

The Board recognizes that the capital markets can be unpredictable at times and that different investment postures could result in periods when the market value of the Fund's assets may decline in value. To protect the Fund's capital, the Board defines risk tolerance as very moderate and infrequent losses over a market cycle (3-5 years).

2. Individual Issues

As a general guideline, the market value of individual positions should not drop 15% relative to the market, as measured by the S&P 500 on a quarterly basis. This is not a *stop loss* limit, but rather a guideline for the Manager(s) who should be prepared to provide sound justification as to why no action was or will be taken to protect capital when stocks fall by the stated percentage relative to the market.

C. Securities Selection and Diversification Policies

In selecting suitable investments for the Fund, certain critical and pertinent elements should be considered by the Manager(s): earnings history, dividend payments, sinking fund provisions, refunding and call privileges, marketability, growth prospects, debt coverage, management, risk, balance sheet strength and degree of leverage.

1. Specific policies and investment restrictions for **fixed income investments**:

a. Fixed income investments should be direct obligations of the United States government, government agencies, or entities that are organized under the laws of the United States of America and the Commonwealth of Puerto Rico and its instrumentalities.

b. There is no limitation as to the degree of participation of the fixed income portfolio in direct obligations of the United States government. However, no more than 50% may be invested in US agencies that do *not* have the full faith and credit of the US Government.

In addition, the following diversification guidelines apply to the maximum allocation allowed in the construction of the Puerto Rico bonds portfolio:

Local Market, Sector/Industry Allocation

	Maximum Allocation
Commonwealth of Puerto Rico and its instrumentalities	100%
Finance (including banks)	40%
Industrial	40%
Utilities	30%

Mortgage Backed Securities:

-Pass-through Collateral	75%
-CMO's	20%

c. The following fixed-income investment alternatives are eligible for investment in the Puerto Rico bonds portfolio: securities issued or guaranteed by the Commonwealth of Puerto Rico and its instrumentalities, securities issued by Puerto Rico corporations and financial institutions, mortgage-backed securities, including CMO's which loans are issued in Puerto Rico, or any other security classified by the Commissioner of Financial Institutions of Puerto Rico as a Puerto Rico asset.

d. Fixed income investments must be rated at the time of purchase within the four highest classifications designated by one of the major rating services, i.e., Standard and Poor's or Moody's Investor Services

e. **No more than 5% of any single debt issue** may be purchased as an investment, with the exception of the US government or its agencies.

f. No more than 10% of the assets of the Fund at market may be invested in the **securities of a single issuer**, with the exception of the US government or its agencies.

g. The management of fixed income investments will be active. This means that when a security can be sold to the long-term benefit of the Fund, it will be. Bonds may also be swapped in order to take
advantage of yield spreads between various qualities of bonds or the yield curve, which differentiates bond returns by maturity. On occasion, securities will be sold at a loss if alternative investments would add to the value of the Fund

and would recuperate the loss in a reasonable period of time. It is believed that safety of principal should not be imposed on each individual investment, however. Instead, the portfolio, taken as a whole, should, over the long term, conserve the purchasing power of the principal and comply with stated objectives.

h. Holdings of individual issues shall be large enough for easy liquidation.

i. Each Manager should maintain a modified adjusted duration for the portfolio under his or her management of +/- 20% the modified adjusted duration of his or her assigned benchmark index. Measurement of modified adjusted duration may include the use of "option-adjusted" analysis for bonds with imbedded options.

j. The modified adjusted (average) duration of the fixed income portfolio should not exceed 7 years. The Fund shall never show an average maturity of 12 years or an average effective maturity in excess of 8 years. The Fund should not purchase any security with an effective maturity of more than 30 years, a duration of more than 15 years or a modified adjusted duration of more than 12 years.

2. Specific policies and investment restrictions for **equity investments:**

a. Securities investments will be, for the most part, of corporations that are created under the laws of the United States. See Section VIII. A limited portion of the equity portfolio, however, shall be assigned for investment in international stocks for diversification purposes.

b. Stocks owned by the Fund should be those traded on the major national and international exchanges or the NASDAQ *over the counter* market.

c. In general, stocks owned by the Fund will be of companies with a market capitalization greater than $1 billion. Up to 15% of the equity portfolio may contain stocks of companies with a market capitalization of less than $1 billion, but not less than $200 million, at time of purchase. In general, stocks owned by the Fund shall have good liquidity, and should not be considered speculative investments.

d. The Fund's position in a single stock will not exceed 5% of the Fund's assets. Also, the Fund's position in a single stock will not exceed 5% of the outstanding stock of any firm.

e. In general, the Fund's equity portfolio shall not be unduly concentrated in any one industry or economic sector. The total portfolio's sectors weights shall not exceed 35% in any one sector. The Fund may invest from time to time more than 35% in an economic sector, up to 40% provided such amount over 35% is justified in writing.

f. On occasion, the Fund will sell a stock at a price below the cost to the Fund. Although the Board avoids the incurrence of losses, these will be tolerated when alternative investments would provide a higher return and permit the loss to be recuperated within a reasonable period of time. It is believed that safety of principal should not be imposed on each individual investment, however. Instead, the portfolio, taken as a whole, should over the long term, conserve the purchasing power of the principal and comply with the stated objectives.

3. Specific policies and investment restrictions for **International (non-US and non-Puerto Rico Investments:**

   a. The fund may invest up to 15% of its assets in securities issued outside the United States of America and/or outside Puerto Rico.

   b. Investments in foreign securities (both equity and fixed income securities) shall consist mainly of securities of companies, governments or entities domiciled in countries considered to be "developed economies and emerging market economies" as defined by the countries that are included in the MSCI All Country World Index ex USA, plus Canada. A portion of up to 50% of the international portfolio can be invested in emerging markets.

   c. Foreign or international equities shall be invested through the use of American Depository Receipts (ADRs) of the publicly traded securities of the countries stated above.

d. International fixed income securities must honor the investment criteria mentioned in Section IX C-1 and international equities must honor the investment criteria mentioned in Section IX C-2.

e. The international equity and/or fixed income managers may utilize the investment technique of active hedging in an effort to protect the international portfolio from possible erosion of capital due to currency fluctuations. The Manager(s) shall exercise full discretion as to the degree and frequency of the currency hedging. However, ACAA and its Board will evaluate the results of such hedging and such strategies shall be analyzed from a risk management perspective, not a return enhancing perspective (ie. hedging shall be performed to control risk, and shall not be speculative in nature). ACAA understands that currency hedging might be even more important in the international fixed income securities, which produce a large portion of their return in the form of coupons paid out in foreign currencies.

4. Specific policies and investment restrictions for <u>real estate investments:</u>

a. ACAA and its Board recognize that real estate investments are less liquid than publicly traded bonds and equities. Investments in real estate and real estate investment vehicles, such as real estate limit partnerships and real estate investment trusts, usually require strict time commitments where the investor (in this case ACAA) may not be able to sell its investment or receive back the amounts invested until years later. It is common for investments in real estate not to return principal until after the fifth year, and may take up to 12 years to do so. The return of principal is usually subject to the sale of the underlying properties, which may take some time. Interest and dividends are usually not guaranteed either, and depend on whether the properties are rented or not. Due to the illiquid nature of this type of investment, the amounts allocated to real estate investments are limited and may not exceed 7% of the fund.

b. As with any type of investment, there are risks, such as the liquidity risk involved in investing in real estate. Nevertheless, real estate investments historically have proved to be valuable diversification tools, with low correlation to other asset classes such as stocks and bonds. **Diversification is one of the main reasons why ACAA has dedicated a portion of its investments to real estate.**

c. Due to the fact that diversification is important, **real estate investments shall include a portfolio of several properties, diversified by geographical region, property type (residential, commercial, industrial, retail, etc,), value of each property, etc.** Diversification has many advantages, including reducing, to some degree, the liquidity risk.

Investments in real estate shall be done through a firm or partnership specializing in these types of investments and shall be done in a professional manner. Real estate investments require very specialized knowledge and expertise, including knowledge of the different property markets (residential, retail, industrial and office markets), geographical and location issues, expertise in drafting or evaluating the contracts with the entities leasing or renting the properties, and many other specialized issues. **The firm(s) or partnership(s) hired to supervise ACAA's investments in real estate shall have a proven track record of these types of investments and should be able to document and share with ACAA the analyses and rationale for the investment decisions made.**

6. Specific policies and investment restrictions for **<u>Cash Equivalents</u>** not invested in the short-term investment fund sponsored by the custodian.

The cash reserve of the Fund is maintained in high quality, short-term investments. Commercial paper, treasury obligations with one year or less remaining to maturity, short-term certificates of deposit (not exceeding 180 days), bankers' acceptances, and repurchase agreements are all permissible investments. The Manager(s) will utilize the investment instruments it regards as the most secure and having the best return. The weighted average maturity of the cash portfolio shall not exceed 90 days.

In any case, however, **commercial paper must be rated A1/P1 by Standard and Poor's and/or Moody's Investor Services.** In addition, bank certificates of deposit must be of institutions rated among one of the top three rating categories by Bank Watch (A, A/B-, or B-).

7. General

The financial securities markets are constantly changing. Not only are the markets volatile from a valuation perspective, but also new types of investment services and techniques are continually being introduced to institutional investors. In recent years interest has developed for such concepts as option writing, market index futures, portfolio immunization, portfolio insulation, depository trusts, and securities lending. Within the coming years, new investment concepts, no doubt, will be defined and offered to institutional investors. The Board should review new investment practices to examine their applicability to the Fund. The same prudence that is exercised when the Fund assumes a new instrument should be used to review the value of new investment practices. New practices are examined from the standpoint of risk and return as well as whether they present a practical advantage to the Fund.

X. Review Meetings and Communications

A. The Board is to meet at least annually with the Manager(s) and quarterly with the Consultant in order to review the progress made in the implementation of this policy. The Board should receive written reports from the Manager(s) on a quarterly basis.
Other communication or meetings between the Board and the Manager(s) will be as warranted.

B. Guidelines related to the on-going monitoring of the Money Managers

The Investment Consultant and ACAA will supervise the work done by the Money Managers. Some guidelines that may be considered when analyzing each manager's work include:

1. Quarterly performance will be evaluated to test progress toward the attainment of longer-term targets. It is understood that there are likely to be short-term periods during which performance deviates from market indices. During such times, greater emphasis shall be placed on peer-performance comparisons with Money Managers employing similar styles.

2. On a timely basis, but not less than four times a year, the Board will meet to focus on:
Money Manager's adherence to the IPS guidelines specific instructions; material changes in the Money Manager's organization, investment philosophy and/or personnel; and,
Comparisons of the Money Manager's results (risk, performance) to

appropriate indices and peer group specifically:

3. The risk associated with each Money Manager's portfolio, as measured by the variability of quarterly returns (standard deviation), must not exceed that of the benchmark index and the peer group without a corresponding increase in performance above the benchmark and peer group.

4. In addition to the information covered during the quarterly reviews, The Board and the Investment Consultant will meet at least annually to focus on:

   - The Money Manager's performance relative to Money Managers of like investment style or strategy. Each Money Manager is expected to perform in the upper half of the Money Manager's respective style universe on an annualized basis.

     The ACAA portfolio performance results with each Money Manager compared to that Money Manager's overall composite performance figures to determine unaccounted for dispersion between the Money Manager's reported results and ACAA's actual results.

5. The Board is aware that the ongoing review and analysis of Money Managers is just as important as the due diligence implemented during the Money Manager selection process. Accordingly, a Money Manager account will be analyzed in more detail upon the occurrence of any of the following:

   A Money Manager performs, on several occasions, in the bottom quartile (75th percentile or lower) of their peer group over quarterly, or annual periods.

   - A Money Manager falls in the southeast quadrant of the risk/return scatter plot for 3- and/or 5-year time periods.

   - A Money Manager, for several quarters, has a 5-year risk adjusted return fall below that of the median money manager within the appropriate peer group.

6. Furthermore, issues which may require the replacement of a Money Managers include:

   - Failure to follow the guidelines established in this Investment Policy

- Money Managers that consistently perform below the median (50th percentile) of their peer group over rolling three-year periods.

- Money Managers who perform below the median (50th percentile) of their peer group over a five-year period.

- Money Managers with negative alphas for 3- and/or 5-year time periods.

- Administrative proceedings by SEC against money managers

7. Major organizational changes also warrant immediate review of the Money Manager, including:

   - Change in professionals involved in the investment process
   - Significant account losses
   - Significant growth of new business
   - Change in ownership

The performance of the ACAA's investment Money Managers will be monitored on an ongoing basis and it is at the Board's discretion to take corrective action by replacing a Money Manager if they deem it appropriate at any time.

Certified by:

Héctor Ramos
Secretary
Board of Directors

Amended April 27, 2012