



Virginia Government Finance Officers' Association – Spring Conference – Arbitrage Management

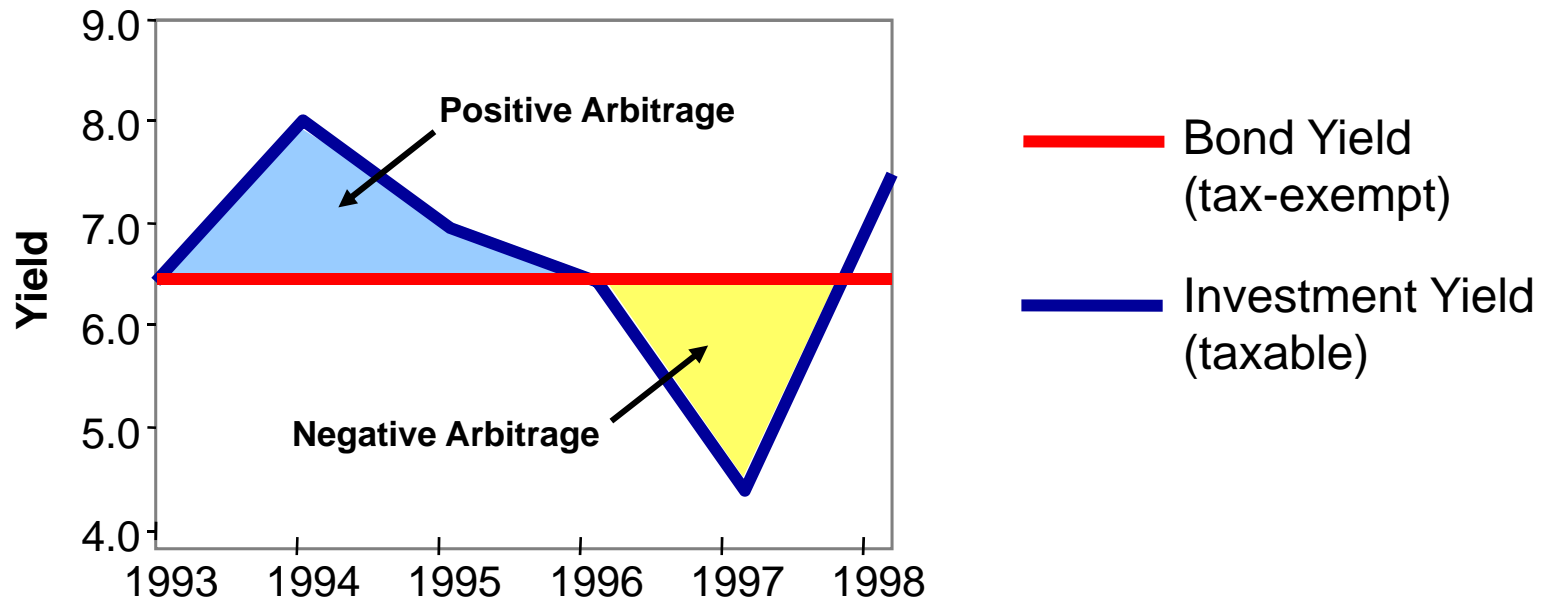
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PFM Asset Management LLC
4350 N. Fairfax Drive, Suite 580
Arlington, VA 22201
(703) 741-0175
www.pfm.com

Presented By:
Nelson L. Bush, *Senior Managing Consultant*

What Is Arbitrage?



Arbitrage is the difference between the rate at which the proceeds of a tax-exempt bond issue were borrowed and the rate at which the proceeds were invested

Exceptions From Rebate



- Small Issuer Exception
 - Issuer must have general taxing powers
 - Issues less than \$5 million or \$15 million for public schools
- Spending Exception (includes earnings)
 - 6-Month
 - 18-Month
 - Two-Year Construction
- Exception from Rebate does not satisfy Yield Restriction requirements

Calculation & Filing Requirements

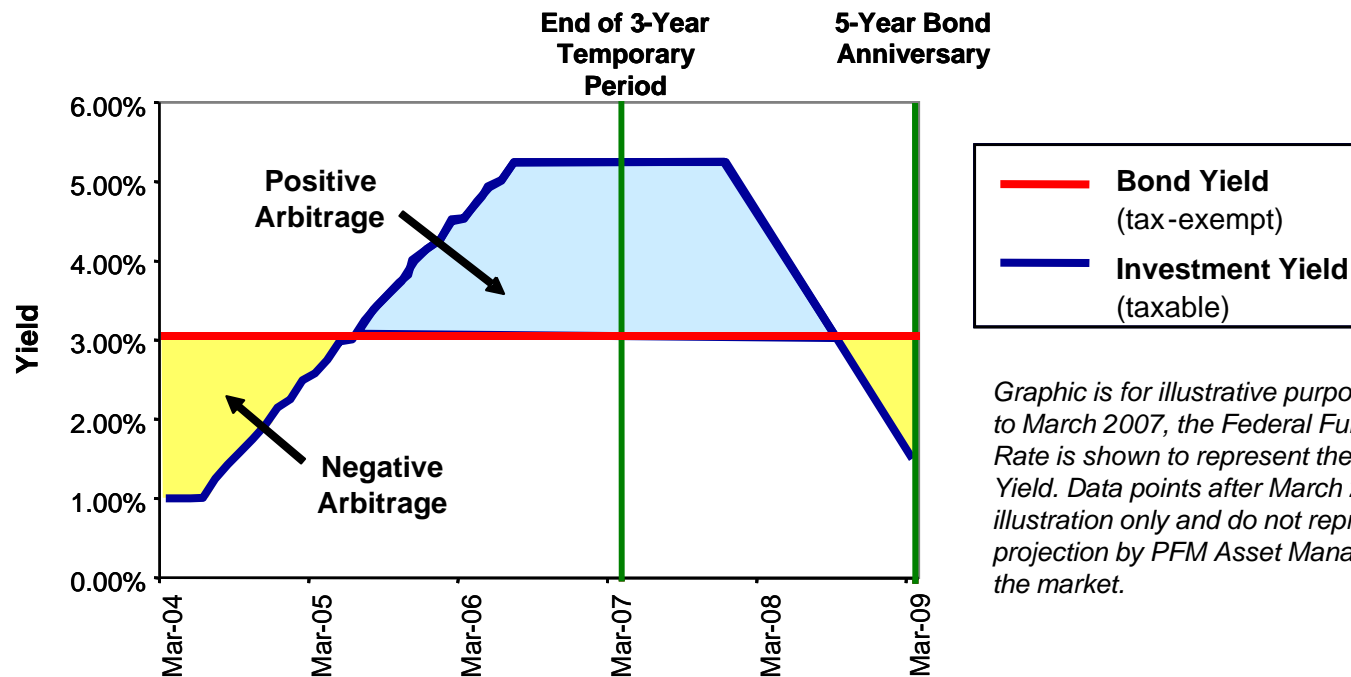


- Rebate payments must be made no later than 60 days after the computation date
 - No later than 5 years after the issue date, and every 5 years thereafter until the final maturity date or earlier redemption date
 - For interim rebate computation periods, issuer required to pay at least 90% of the rebate liability
 - As of final computation period, issuer required to pay 100% of rebate liability
- Form 8038-T
- Issuer **does not have to file a** rebate report

Arbitrage Rebate vs. Yield Restriction



- Earnings on tax-exempt bond proceeds are restricted for:
 - The life of the bonds (Arbitrage Rebate)
 - Periods after the Temporary Period (Yield Reduction Payment)
- Separate calculations
- There may be instances, at the end of a fifth bond year anniversary, when an issuer does not owe rebate, but must make yield reduction payments



Graphic is for illustrative purposes only. Prior to March 2007, the Federal Funds Target Rate is shown to represent the Investment Yield. Data points after March 2007 are for illustration only and do not represent a projection by PFM Asset Management LLC or the market.

- Tax-exempt bond proceeds must be “yield restricted” to a rate that is not materially higher than the yield on the bonds
- Typically, “materially higher” means one-eighth of one percent (0.125%).
- Some funds are NOT subject to yield restriction:
 - Project funds that qualify for the 3 or 5 year temporary period.
 - Interest earnings - unrestricted for 1 year
 - Debt service funds - unrestricted yield for 13 months
 - Reserve fund - unrestricted for life of issue
- A temporary period is an exception to yield restriction, not an exception to arbitrage rebate

- The **SNAP Program** offers a complete package of services:
 - Professional investment management
 - Security custody services
 - Portfolio accounting
 - Arbitrage rebate compliance tracking and reporting
 - Comprehensive website with online account access
 - Educational sessions and workshops
 - Toll-free customer service line

SNAP Service Providers

Oversight	Virginia Treasury Board
Investment Manager and Administrator	PFM Asset Management, LLC
Rebate Calculation Agent	Pinnacle Arbitrage Compliance, LLC
Custodian / Depository	U.S. Bank N.A./ Wachovia Bank, N.A.
Program Counsel	Sidley Austin LLP

SNAP Rebate Services



Service*	Description	Timing
Rebate Estimate	Rebate estimate prepared following IRS future value calculation methodology	Each June 30 and as requested
Preliminary Expenditure Exception Compliance Calculation	Estimated projection of compliance with applicable spend down exception including calculation of any expenditure deficiency	30 days before expenditure test date
Expenditure Exception Compliance Report	Estimated report of compliance (or failure to comply) with expenditure exception	Within 30 days after expenditure test date
Penalty Calculation	Estimated calculation of “payment in lieu of rebate” due, if elected	Within 30 days after expenditure test date
Final Rebate Calculation	If requested, Formal Rebate Calculation Report	Installment Computation Date or as requested

* All reports and tracking are at no additional charge except for the Formal Rebate Calculation which can be provided by the Program’s Rebate Calculation Agent, Pinnacle Arbitrage Compliance, LLC.

Rebate Related Suggestions



1. Spend proceeds with diligence
2. Understand the project schedule and provide it to the investment manager
3. Reimburse the General Fund regularly for project expenditures
4. Review rebate reports
5. Establish a Rebate Account
6. Inform investment manager of projects that are funded by multiple issues
7. Inform investment manager and rebate agent of any refunding issues
ESPECIALLY if they refund short term notes or interim financings
8. If possible, keep Bond Resolution general
9. If possible, spend earnings during project
10. SPEND PROCEEDS

Important Disclosures and Disclaimers



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*The SNAP Fund is a series of the Commonwealth Cash Reserve Fund, Inc. An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other governmental agency. Although the Fund seeks to preserve the value of investments at \$1.00 per share, it is possible to lose money by investing in the Fund. **PFM Fund Distributors, Inc.**, member of the Financial Industry Regulatory Authority (FINRA) (www.finra.org), serves as the Fund's Distributor. PFM Fund Distributors, Inc. is a wholly owned subsidiary of PFM Asset Management LLC.*