



Florida PRIME™ Best Practices Review

Florida State Board of Administration (SBA)

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Executive Summary

Aon Investments (Aon) conducts a Best Practices Review of Florida PRIME on an annual basis. In this report, we review the 2023 Participant Survey responses, provide a review of our onsite visit to Federated Hermes, provide an update on participant communication, and recap the annual Investment Policy Statement Review.

Based on our review, we continue to believe that Florida PRIME is being managed in a manner consistent with best practices and in consideration of participants' best interests. We do not have any recommendations as a result of this review.

2023 Participant Survey Highlights

On a regular basis, the SBA conducts a survey of Florida PRIME participants to gain a better understanding of the participant base, current usage of available services, and overall satisfaction. The survey also seeks to gauge interest across several factors and to ensure awareness of participant needs and preferences.

During the release of the 2022 survey, a technical glitch prevented reminder emails to be sent to participants and only 11 responses were received. Therefore, the Participant survey was resent in the Fall of 2022 and received 39 responses. This is closer to a more normal response rate, though lower than previous years which is not unexpected given the circumstances.

A diversified group of governmental units responded to the survey, primarily representing counties, special districts, municipalities, and school boards, with respondents roughly evenly split between investment decision-makers and personnel in account operations. Of the respondents, 44% have one account with Florida PRIME and 21% have 2 accounts. The survey indicated that approximately 65% of respondents have a balance of over \$10 million with Florida PRIME, and another 16% indicated having between \$1 million and \$10 million with the pool. These numbers are generally in line with previous surveys.

The survey includes questions that relate to how and why participants utilize other competing and complementary liquidity vehicles. Of the respondents, over 65% indicated that their organization has a policy that dictates a maximum allowable allocation to a single investment pool or money market fund. Of those with a policy limit, approximately 65% are restricted to allocating 50% or less to any single governmental investment pool or money market fund. Relatedly, when asked what prevents an organization from using Florida PRIME as the primary source of cash management, 28% indicated that investment policy restrictions are a major reason and another 13% indicated it is a moderate reason. The greatest response was 46% of respondents who indicated that diversification needs of the cash portfolio was a major or moderate reason. The aggregated responses did suggest that an unattractive current yield was not much of a reason, which was slightly different than previous years. Inadequate participant disclosures, costs, functionality/operational features and lack of additional investment product offerings were all highly selected as not reasons at all for not using Florida PRIME as a primary source of cash management.

When asked about other investment vehicles used in the past 12 months for cash management, respondents indicated the most used vehicle aside from Florida PRIME is an SEC registered money market fund at 52%. The next most common vehicle was peer fund, the Florida Education Investment Trust Fund at 35%, followed by Bank Certificates of Deposits at 30% of respondents. These results are like previous years. The survey also asked respondents to rank how competing investment services have added value to the respondent organizations' investment goals. Consistent with last year, respondents

indicated that yield was the most appealing feature, followed by risk, defined as perceived risk levels adjusted for the level of return. Ease of use and cost were ranked the lowest in terms of value add from competing investment services, followed closely by client service and available funds.

The survey questions surrounding current services related to Florida PRIME continue to receive strong feedback. Related to the Florida PRIME website, 79% of respondents indicated that they visit the site at least once a month and 100% responded that they find the website functionality as very easy to use. The survey also indicated that the majority of participants continue to utilize the website primarily to access account balances/statements and transactions, and approximately 45% of respondents utilize the website to access the Monthly Summary Reports. When asked about the usefulness of multiple communication pieces, the responses also continue to be favorable. The survey indicated that respondents rated the following communications as very useful: monthly account statements (95%), e-mail notifications of withdrawals (80%) and changes to bank instructions (79%). Further, respondents found the following to be at least somewhat useful: Periodic eNotices (45%), Monthly Summary Reports (24%), and Weekly Market Commentary (58%). Lastly, respondents indicated fantastic satisfaction with the Florida PRIME representatives, with 100% of respondents indicating the representatives were very courteous, very knowledgeable and very responsive.

Overall, the survey results continue to be positive from both operational and service-related perspectives. Responses related to the use of competing investment vehicles continue to indicate SEC money market funds as the primary vehicle, with indications of yield and risk being top of mind, but notably, that a large percentage of respondents' organizations have investment policies limiting available funds to invest in a single entity and/or seek diversification from a single cash management source. Generally, the survey indicates a strong level of satisfaction with the management of the Florida PRIME portfolio. The large majority (98%) of respondents indicated that they are very likely or extremely likely to recommend Florida PRIME to a colleague or other governmental investor. We continue to believe the survey is a great mechanism to obtain feedback from Florida PRIME participants, as well as to express the SBA's awareness and receptiveness to the participant's needs and wants.

Federated Hermes Onsite

The SBA contracts Federated Hermes (“Federated”) to provide investment services for Florida PRIME and therefore it is crucial to maintain an up-to-date understanding of the business and favorable outlook on a go-forward basis. The objective of the onsite due diligence meetings is to conduct a comprehensive review of Federated’s business, personnel and processes, and specifically those that directly impact the management of the Florida PRIME portfolio. Aon and SBA Staff conduct onsite meetings at Federated’s offices on a periodic basis. The prior visit occurred in April 2017 and thus, it was determined an onsite visit was due to be completed. SBA Staff and Aon representatives went onsite to Federated’s headquarters in Pittsburgh, PA on April 19, 2023.

Attendance at the meeting included the Senior Officer of Investment Programs & Governance and the Chief Risk and Compliance Officer at the SBA and from Aon a fixed income researcher and general consultant relationship manager. The meeting included dedicated time with fourteen senior Federated professionals from multiple areas of the firm and included time with President & CEO, Chris Donahue, and President of Federated Securities Corp., Paul Uhlman. Additionally, the key personnel that touch the Florida PRIME portfolio daily were present for the duration of the meeting, including the relationship manager, portfolio manager and head of trading.

We continue to find Federated to be among the most highly regarded money market managers in the industry. The most recent onsite meeting reinforces our confidence in Federated’s capabilities of managing the Florida PRIME portfolio, staying apprised and ahead of the ongoing changes in the money market and related industries, and importantly, safeguarding the assets of the pool’s participants. The Federated team is a long-tenured leader in the local government investment pool arena, is responsive to the needs of Florida PRIME and is a proven partner for the SBA.

Below we provide a brief summary of the agenda topics and the surrounding discussion.

Corporate Overview

As previously reported, Federated Investors acquired a majority interest in Hermes Investment Management, a London-based firm, in July of 2018. The acquisition was complimentary in nature to legacy-Federated’s business and had little impact on the services provided for FL PRIME. Federated continues to be a highly regarded institutional money market fund manager and a leader in liquidity and fixed income management. As of December 31, 2022, the firm had \$668.9 billion in assets under management and 1,961 employees. Approximately 70% of the assets managed are liquidity assets and over 20% are managed in Treasury Pool assets which highlights the focus of the firm’s capabilities. Additionally, the firm manages assets across all 50 states, and specifically local government investment pools (LGIPs) in 38 states, which speaks to their experience serving investors like Florida SBA. Also of

importance is that Federated's revenue sources are diversified across money market, fixed income, equity, and recently alternative/multi-asset investment products through the Hermes acquisition.

Federated employs a deep team of 120 liquidity and fixed income investment professionals, including 48 portfolio managers, 46 analysts and 26 traders. The portfolio management team averages 21 years of experience and 16 years at Federated, speaking to the team's stability and experience. Additionally, the firm is active in the industry across multiple venues, evidenced by the conferences attended, market expertise and the in-depth coverage of passed and proposed regulations and rules. This work instills confidence in the guidance and management of the Florida PRIME portfolio. Overall, we find Federated to be a high-quality and proactive player in the money market space with a stable and strong organization.

Enterprise Risk Management

Measurements of Risk / Monitoring / Resolution

The Enterprise Risk Management (ERM) division develops, implements, and maintains the risk management programs for Federated. This covers investment matters, administration, operations and distribution. Importantly, ERM is independent of the Investment Department, with the Chief Risk Officer reporting directly to Chief Legal Officer, who in turn reports directly to the Chief Executive Officer of Federated. Additionally, the team meets independently with the Fund Trustees and Board of Directors. The Chief Risk Officer oversees a robust ERM team and has developed several risk committees which are embedded within each business unit. Each committee develops a charter which is reviewed and updated on a regular basis to ensure the activities and attention of the committee remain appropriate and effective. The committees have developed a systematic scoring process which assesses probability and severity of impact of identified risks. The scoring process allows Federated to assess different strategies and better prepare and manage assets. The risks are dynamically evaluated and reassessed on a regular basis. Additionally, Federated's internal audit periodically reviews the risk committees' processes to ensure their appropriateness and effectiveness.

Cybersecurity Vigilance and Controls

Federated also provided an update on the Firm's Cybersecurity efforts. Federated's Information Security Group team is comprised of eight individuals who report to the Information Security Manager, who in turn reports to the Director of Cybersecurity and ultimately to the Chief Information Security Officer. Federated's cybersecurity program The Cybersecurity Framework aligns with the National Institute of Standards and Technology (NIST) framework, it is robust with multiple layers of security and regular internal and external evaluations. All employees are required to take cybersecurity awareness course and anti-phishing training and cybersecurity awareness is factored into employees' performance evaluations.

Business Continuity

Federated's Business Continuity team manages the communications network and information technology infrastructure. Security of client and Federated information is managed at multiple levels at the firm. The Firm has dedicated Business Continuity committees that report directly to the Director of Technology.

Federated utilizes a dual data center architecture located on separate power grids to support the business and each are designed for 100% daily workload capacity. All satellite offices connect to both data centers, reducing risk by allowing all critical daily functions to run smoothly in the event of an emergency. Federated has several business continuity plans throughout the company which are tested on an annual basis. Additionally, Federated reviews all third-party organizations they partner with to ensure information and data is handled in an appropriate and secure manner, and that their vendors' business continuity plans are up to Federated's standards. Post-Covid, all associates have laptops which provides maximum flexibility for a hybrid work environment and enhances their ability to avoid business disruption. Overall, we find Federated's risk management and information security infrastructure and procedures to be robust and in line with industry best practices.

Portfolio Update

Portfolio Review

Senior Portfolio Manager for the Florida PRIME pool, Paige Wilhelm, led a short discussion on the Florida PRIME portfolio. The pool is managed with the goal of providing safety, liquidity and competitive returns while minimizing risk. Ms. Wilhelm provided an update on the investment strategy, as well as Federated's view of the current and expected money market investment landscape. The Florida PRIME portfolio continues to perform favorably and competitively and has provided the safety and liquidity characteristics needed by its participants. Overall, the Florida PRIME portfolio continues to be managed successfully and in a thoughtful and prudent manner.

Trading

Tracey Lusk, Head of Global Liquidity Markets lead the discussion on Federated's trading practices. The Federated trading team is well tenured, with 10 traders dedicated to liquidity portfolios. Each trader is cross-trained which allows them to step in on a different portfolio if needed. The trading process begins with the development of the investment strategy, which is followed by thorough credit analysis before trading takes place. When trading, the team utilizes a best execution policy for selecting brokers and has a committee that meets quarterly and oversees the broker selection practices. All trades are entered into FedPorts, Federated's proprietary order management system, for pre- and post-trade compliance. FedPorts is customized by role in portfolio management (i.e. compliance, trading, credit analysis, portfolio management, etc.) which offers a strong level of compliance. Trading Operations is separated from the trading functions and monitors all trades from initiation through settlement and confirms trade details with counterparties. The trading team works together with Federated's other business units to execute Florida PRIME's investment strategy on a seamless basis.

Compliance

The Federated Compliance Department is responsible for the development of compliance programs for the investment management function and monitors investment activities and operations for compliance with applicable regulations, client guidelines and corporate standards.

Specific to Florida PRIME, this team is responsible for monitoring the portfolio's investment activities and operations for compliance with the Investment Policy Statement and applicable guidelines, such as GASB 79. The Compliance Department, in conjunction with the Business Information Services Division (BISD) and Global Investment Operations (GIO) develop, update, and implement automated tests within the trading system to assure trading compliance with Policy. Proprietary system, FedPorts, allows Federated to create a set of rules specifically for the Florida PRIME portfolio. These rules and automated tests are constantly updated and reviewed to ensure they are in line with the governing policies and regulations of Florida PRIME.

Every trade that is generated runs through compliance. Should any trade placed not comply with the set of rules, a notice of either 'Warn,' 'Fail' or 'Stop' will be received and will need to be rectified before the trade can be processed. Each notice has a different level of importance and corresponding parameter on who can validate the trade.

Overall, we believe Federated has implemented a straightforward and efficient system to ensure guidelines are followed and escalation procedures are effective. The compliance program the Federated Compliance Department has developed has been successful in the management of the investment pool and in maintaining compliance with the applicable Florida PRIME regulations and policy.

Legislation Discussion

Before concluding the meeting, David McCandless, Corporate Counsel for Federated, provided a very comprehensive overview of the relevant legislative landscape. David and his team meet regularly with lawmakers and SEC representatives to offer perspective, insight into the money management business and suggestions on rule or bill proposals. Currently, while there are several proposed bills and rules, it is too early and there is too much uncertainty for any action on the part of Florida PRIME. As has been the case over the years, Federated continues to be a very active participant in the industry and a crucial aide to the SBA in staying current with the relevant rules and regulations, as well as with the guidance and best practices that comes from the Governmental Accounting Standards Board.

Separate Aon Due Diligence

Aon Investments has a team of over 130 individuals dedicated to investment manager research covering traditional and alternative asset classes, including the money market and short-term bond markets. Independent of the Florida PRIME-related Federated due diligence visit, Aon covers Federated from a research and monitoring perspective and specifically has buy-rated two of Federated's money market strategies (Government Obligations and Prime Obligations funds). The Florida PRIME portfolio has, from time-to-time invested in these funds periodically to manage short-term liquidity needs. A buy-rating from Aon means that the strategy has gone through a very comprehensive quantitative and qualitative due diligence process that includes review of the following seven key factors: business, team, process, risk management, performance, terms & conditions, and operational due diligence. While this due diligence is

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not specific to Florida PRIME, it is relevant and reinforces our conviction in Federated Hermes' ability to manage participants' assets prudently and effectively.

Conclusion

The onsite meeting provided a comprehensive overview of the firm and access to Federated's senior professionals. The meeting reinforced our confidence in Federated's capabilities with regard to the people, processes, risk management and technology that support the management of Florida PRIME and we continue to have confidence in Federated's ability to manage and safeguard the assets of Florida PRIME participants.

Communication Update: Banking and Financial Sector

Among the strengths of Florida PRIME is the level of communication with participants and transparency into the management of the asset pool. During the first quarter of 2023 as the regional banking crisis was playing out in the U.S, Federated Hermes was proactive in offering commentary around the situation and specifically context for the Florida PRIME portfolio's investments.

In addition to the weekly commentary, Federated posted additional and timely updates on exposure to the failed banks (zero exposure) and context around Florida PRIME's investments. Importantly, the communication piece posted March 31st and titled "Market Update on the Banking and Financial Service Sectors" reminded readers of Florida PRIME's goals and objectives, as well as the makeup of the investment opportunity set. The importance of this piece was to remind participants that Florida PRIME is focused on the safety, liquidity, and competitive returns with minimization of risks, which means investing in short-term, high-quality securities. The link to the current events is that the bank and financial services sector is responsible for a large supply of securities in money markets, primarily through commercial paper, certificates of deposits and repurchase agreements. These offerings meet the high standards for investment and thus Florida PRIME has roughly two-thirds of its assets invested in securities tied to the sector. The communication piece put this in perspective noting that the prime money fund industry holds between 40-80% in the banking and financial services sector.

We highlight this commentary as it is an ongoing reminder of the comprehensive, prudent and transparent management of the Florida PRIME portfolio. The communication offered participants 1) transparency into the portfolio's holdings in light of the market situation, 2) context related to money markets and specifically the large presence of the bank and financial services sector and 3) assurance that the goals and objectives of Florida PRIME are at the forefront of investment decisions.

Investment Policy Review

As part of Aon's Best Practices Review we conduct a review of the Florida PRIME Investment Policy Statement (IPS). The objective of the IPS is to set forth the objectives, strategy, guidelines, and overall responsibilities for the oversight and prudent investment of Florida PRIME assets. The purpose of the periodic review is to ensure the document reflects the evolving investment portfolio, current legal and regulatory developments, and best practices. A well-written and unambiguous document is critical to the success of any investment program.

Following the 2023 review, Aon continues to find the IPS to be comprehensive and appropriate for the management and oversight of Florida PRIME. The topics covered continue to be relevant and critical to the success of the management of the pool's assets. The investment objective of the pool and the roles and responsibilities are clearly defined. The IPS provides the necessary specifics and supplemental guidelines for a clear understanding of the investment strategy, making direct and clear reference to the appropriate GASB guidelines for appropriate fiduciaries to follow and understand. We believe the IPS thoroughly defines the risks that are associated with investing in Florida PRIME and find the detailed control procedures provide the comfort of prudent safe-keeping and oversight of assets. The SBA has been diligent with staying current with overall best practices in managing the Florida PRIME assets and has consistently ensured the IPS is up to date with the current regulatory, legal, and investment environments.

Overall, we continue to believe the Florida PRIME IPS is robust and in line with the goals and objectives of the investment pool and continue to find the Policy to be an effective guiding document for the management of Florida PRIME.