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Repurchase Agreements – Benefits, Risks and Controls

A repurchase agreement (repo) is an agreement between two parties whereby one party sells the other a security at a specified price with a commitment to buy the security back at a fixed time and price. Maturities can vary from overnight to a year, with the longer-maturity repos commonly referred to as “term” repos.

The repos that Columbia Management enters into are known as “tri-party” repos. In these arrangements, a custodian bank acts as an intermediary between the two parties and creates operational efficiencies by providing, among other things, standardized legal documentation, transaction settlement services and collateral segregation. Tri-party repos generally provide yield enhancement while also reducing the overall risk of the transaction.

Repos are widely used by the managers of money market funds because they generally offer three distinct benefits:

- **Liquidity** – Repos provide the ability to invest cash overnight, making them a critical component in the effort to manage liquidity.
- **Yield Advantage** – Repos generally provide additional yield as compared to traditional money market instruments, such as Treasury bills, time deposits or agency discount notes. The yield advantage depends on such factors as the repo’s maturity dates and the credit quality of the repo’s collateral.
- **Flexibility** – The principal amount of repos can be adjusted up or down as fund cash flows dictate.

Repos are generally designed so that if a counterparty fails to perform its obligations under the repo, the fund takes possession of the collateral. While counterparty selection and collateral requirements provide the fund protection, repos remain subject to counterparty risk. If a counterparty defaults, a loss may be realized on the sale of the underlying security to the extent that the proceeds from the sale and accrued interest of the security are less than the resale price provided in the repurchase agreement, including interest. Moreover, should a counterparty declare bankruptcy or become insolvent, a fund may incur delays and costs in selling the underlying security or may suffer a loss of principal and interest. This could occur, for example, if a fund is treated as an unsecured creditor and is required to return the underlying collateral to the counterparty or its assigns.

Columbia Management seeks to mitigate risk by providing credit and portfolio oversight through controls and reviews that include:

- **Credit Review Process** – Columbia Management’s assessment of credit quality includes:
 - Screening of counterparties by internal credit analysts whose recommendations are reviewed by Columbia Management’s Credit Review Committee (CRC). If approved by the CRC, the counterparties are then added to an approved issuers list. A fund typically will enter into repurchase agreements only with commercial banks, registered broker/dealers and the Fixed Income Clearing Corporation.
 - Monitoring of the CRC’s approved issuers list by Columbia Management’s Investment Oversight Committee (IOC). The IOC includes Columbia Management’s president, chief investment officer and the heads of equity, fixed income and cash investments, as well as representatives from legal, risk and compliance.
- **Collateral Requirements** – Columbia Management’s collateral requirements designed to protect fund investors should a counterparty default include:

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- The value of the security must be greater than the value of the repo itself (from 102% to 105% of the repo value depending on the collateral's credit quality).
- Repo positions must have first claim and priority lien on the collateral, which is held by third-party custodian banks.
- **Operating Controls** – Columbia Management conducts periodic reviews to verify that the requirements noted above are met and that the appropriate legal agreements are in place to protect a fund's interests in the collateral.

Columbia Management believes its credit review process, collateral requirements and operating controls are reasonably designed to manage counterparty risk associated with repos. As such, Columbia Management continues to believe that repos are an appropriate investment vehicle for the funds it manages.

Please read and consider the investment objectives, risks, charges and expenses for any fund carefully before investing. For a prospectus, which contains this and other important information about the fund, contact your Columbia Management representative or financial advisor or go to www.columbiamanagement.com.

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