METROPOLITAN WATER RECLAMATION DISTRICT OF GREATER CHICAGO

INVESTMENT POLICY

Adopted 12/16/99
Revised 4/12/01
Revised 7/8/10

PREAMBLE

It shall be the policy of the District that all public funds available, not restricted by immediate need, be invested in investment securities so as to maximize return without sacrifice of safety or necessary liquidity.

I. Scope

This policy applies to the investment of monies in Capital Funds for construction, Operating Funds and Debt Service Funds of the Metropolitan Water Reclamation District of Greater Chicago (the "District").

II. General Objectives

The primary objectives of investment activities, in priority order, shall be safety, liquidity, and yield:

1. *Safety*

Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk and interest rate risk.

a. Credit Risk

The District will minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

i. Limiting investments to the safest types of securities.
ii. Pre-qualifying through size, reputation, experience and history, the financial institutions, broker/dealers, intermediaries, and advisers with which the District will consider doing business.
iii. Diversifying the investment portfolio so that potential losses on individual securities will be minimized.
iv. Collateralization of investments when appropriate with United States Government Securities or Irrevocable Letters of Credit issued by the Federal Home Loan Bank (FHLB) at 105% or 102% of market value, respectively, excluding the amount insured by the FDIC.

b. Interest Rate Risk

The District will minimize the risk that the market value of securities in the portfolio will fall due to changes in market interest rates by:

i. Structuring the investment portfolio so that sufficient securities mature to meet cash requirements for ongoing operations, construction and debt service, thereby avoiding the need to sell securities on the open market prior to maturity in order to meet current cash needs.

ii. Investing operating, construction and debt service funds needed for expenditure within thirty days in short-term securities, interest-bearing savings accounts, money market mutual funds, the Illinois State Treasurers' Illinois Funds Investment Pool, and such similar investment pools as may be authorized by the Illinois State Legislature.

iii. Longer term investment of funds not needed within thirty days, to meet general dates of projected future expenditure needs, in securities, both interest-bearing and discount obligations of the United States Government and its agencies created by Acts of Congress; Commercial Paper up to a maximum of 270 days; Bank Certificates of Deposit collateralized by United States Government securities or Irrevocable Letters of Credit issued by the Federal Home Loan Bank (FHLB) at 105% or 102% of market value, respectively, excluding the amount insured by the FDIC; Municipal Bonds of state and local governments rated as investment grade by two of the four national rating agencies; and Certificate of Deposit Account Registry Service (CDARS) investments.

2. *Liquidity*

The investment portfolio shall be kept sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by structuring the portfolio so that securities mature concurrent with anticipated cash needs (static liquidity). Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist, to a sufficient degree, of securities with active secondary or resale markets (dynamic liquidity). A portion of the portfolio also may be placed in money market mutual funds or state or local government investment pools which offer same-day liquidity for short-term funds.

3. *Yield*

The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core of investments is limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed. Securities shall not be sold prior to maturity, with the following exceptions:

a. A security with declining credit may be sold prior to its stated maturity in order to minimize loss of principal.

b. A security exchange through sale and purchase that would improve the quality, yield, or target duration in the portfolio or secure a profit at sale without sacrifice of safety and with a net gain in interest income realized.
c. Liquidity needs of the portfolio require that the security be sold.
d. When required to comply with provisions of laws, regulations, grants and contracts including, but not limited to IRS regulations, federal and state statutes, grant agreements and bond indentures.

III. Standards of Care

1. *Prudence*

The standard of prudence to be used by investment officials shall be the "prudent person" standard and shall be applied in the context of managing an overall portfolio. The Treasury Analyst, Assistant Treasurer, and the District Treasurer, when acting in accordance with written procedures and this investment policy, and exercising due diligence, shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and the sale of such securities are carried out in accordance with the terms of this policy.

Investments shall be made with such 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.

2. *Ethics and Conflicts of Interest*

The Treasurer, Assistant Treasurer, Treasury Analyst and any other employees, including the Board of Commissioners, involved in the investment process shall abstain from any personal business activity that could conflict with the proper execution and management of the investment program, or that could impair their ability to make impartial decisions. They may have no financial interest, direct or indirect, in any financial institution designated as a depository for District funds. They shall further disclose to the District's Board of Commissioners any personal financial/investment positions that could relate to the performance of the District's investment portfolio. They shall abstain from undertaking any personal investment transactions with the same individuals with whom business is conducted on behalf of the District.

3. *Delegation of Authority*

Authority to manage the investment program is granted to the Treasurer and derived from Illinois Statute 70ILCS, 2605/4.1a., Duties of Treasurer. Ultimate responsibility for the operation of the investment program lies with the Treasurer, but day-to-day operation and investment decisions are hereby delegated to the Treasury Analyst and his directed assistants, who shall act in accordance with the established written procedures and internal controls for the operation of the investment program consistent with this investment policy. The Assistant Treasurer shall monitor all ongoing investment activity, assess markets, provide guidance consultation, and keep the Treasurer informed of market conditions and investment objectives. Written investment procedures should include references to: safekeeping, delivery vs. payment, investment accounting, repurchase agreements, wire transfer agreements, and collateral/depository agreements. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the Treasury Analyst. The Assistant Treasurer shall be responsible for all transactions undertaken by the Treasury Analyst and staff, and shall, with the Treasurer's input and approval, establish a system of internal controls to regulate the activities of subordinate staff employees.

IV. Safekeeping and Custody

1. *Authorized Financial Dealers and Institutions*

   a. A list will be maintained of financial institutions and broker/ dealers authorized to provide investment services. Depository investments will be limited to banks, savings and loan associations, and credit unions, which meet the following criteria:

      i. Banks and Savings and Loan associations must be insured by the Banking Insurance Fund and the Savings Association Insurance Fund of the FDIC, respectively. Credit unions must be insured by the National Credit Union Share Insurance Fund (NCUSIF).
      ii. All depository institutions must have a "Satisfactory" or "Outstanding" Community Reinvestment Act rating.

   b. The District will not have funds on deposit with any depository in an amount that would exceed seventy-five percent (75%) of the institution's capital stock or net worth.

   c. Additionally, authorized and suitable investments may be purchased from broker/dealers listed as "primary" dealers or regional dealers, which includes minority dealers. The broker/dealers will be selected by their creditworthiness as follows:

      i. All broker/dealers must qualify under Securities and Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule).

ii. Dealers must have at least five (5) years in operation, provide quarterly financial reporting, and inform the District of any turnover in officers within the organization.
iii. All broker/dealers must provide a certificate evidencing good standing as Qualified to do Business in the State of Illinois.
iv. All broker/dealers must provide disclosure of the firm used to clear trades with the District. Subject to review and rejection by the District.

d. All financial institutions and broker/dealers who desire to become qualified for investment transactions must supply the following as appropriate:

i. Audited financial statements.
ii. Banks must submit for review Quarterly Report of Condition and Income ("Call Reports") as filed with the appropriate Federal and/or State oversight agency.
iii. Brokers must submit for District review the Quarterly "Focus Report, Form X-17A-5" as filed with the appropriate Federal oversight agency.
iv. Certification of Minority (MBE), Small (SBE), or Women (WBE) Business Enterprise status as applicable.
v. Certification of having read and understood and agreement to comply with the District's investment policy.

e. An annual review of the financial condition and registration of qualified financial institutions and broker/dealers will be conducted by the Assistant Treasurer.

2. *Internal Controls*

The Treasurer and Assistant Treasurer are responsible for establishing a written program of internal controls designed to ensure that the financial investment assets of the District are protected from loss, theft or misuse. The internal control structure shall be designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that 1) the direct and indirect cost of a control should not exceed the benefits likely to be derived, and 2) the valuation of costs and benefits requires estimates and judgments by management.

As part of the statutorily required annual financial audit of the District, a review of investment operations shall be conducted to assure compliance with policies and procedures.

The internal controls shall address the following points:

a. Control of collusion
b. Separation of transaction activity from accounting and recordkeeping activities

c. Custodial safekeeping
d. Avoidance of physical delivery securities
e. Clear delegation of authority to subordinate staff members
f. Written confirmation of transactions for investments and wire transfers
g. Development of wire transfer agreements with banks and third-party custodians

3. *Delivery vs. Payment*

All trades where applicable will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in an eligible financial institution prior to the release of funds. Securities will be held by a third-party custodian and evidenced by safekeeping receipts.

V. Suitable and Authorized Investments

1. *Investment Types*

Funds shall be invested in such securities as authorized by Illinois Public Act 235: Public Funds Investment Act. The following investments will be permitted under this policy, but may be further restricted for additional safety at the discretion of the Treasurer of the District:

a. Bonds, notes, certificates of indebtedness, treasury bills or other securities now or hereafter issued, which are guaranteed by the full faith and credit of the United States of America as to principal and interest.

b. Bonds, notes, debentures, or other similar obligations of the United States of America or any of the following agencies:
    i. the Federal Land Banks, Federal Intermediate Credit Banks, Banks for Cooperative, Federal Farm Credit Banks, or any other entity authorized to issue debt obligations under Farm Credit Act of 1971 (12 U.S.C. 2001 et seq.) and Acts amendatory thereto;
    ii. the Federal Home Loan Banks (FHLB), the Federal Home Loan Mortgage Corporation (FHLMC); and
    iii. any other agency created by an act of Congress.

c. Interest-bearing savings accounts, interest-bearing certificates of deposit or interest-bearing time deposits or any other investments constituting direct obligations of any bank as defined by the Illinois Banking Act or interest-bearing share certificates guaranteed or insured by the NCUSIF.

d. Short-term obligations (Commercial Paper) of corporations organized in the United States with assets exceeding $500,000,000 if:

    i. such obligations are rated at the time of purchase at the highest classification: A1/P1/F1/D1 as established by at least two of the four major rating services (Standard and Poor's, Moody's, Fitch, and Duff and Phelps) and which mature not later than 270 days from the date of purchase;
    ii. such purchases do not exceed 10% of the issuer corporation's outstanding obligations; and
    iii. no more than one-third (33%) of the District's funds may be invested in short-term obligations of corporations.

e. Money market mutual funds registered under the Investment Company Act of 1940, provided that the portfolio of any such money market mutual fund is limited to obligations described in points (a) and (b) above, and to agreements to repurchase such obligations.

f. Short-term discount obligations defined as Federal National Mortgage Association (FNMA), Federal Home Loan Discount Note (FHDN), Freddie Mac Corporation Discount Note (FMCDN), Federal Farm Credit Banks Discount Notes (FCDN and FFCB), Federal Home Loan Bank (FHLB), and Federal Home Loan Mortgage Corporation (FHLMC).

g. The Illinois State Treasurers' "Illinois Funds" (formerly Illinois Public Treasurers' Investment Pool).

h. Repurchase Agreements of U. S. Government securities with banks, trust companies or registered primary reporting dealers authorized to do business in the State of Illinois, for a period up to a maximum of 180 days. A third party custodial institution must be established to hold such securities for benefit of the District for the duration of the specific agreement.

i. Municipal Bonds of any county, township, city, village, incorporated town, municipal corporation, or school district, of the State of Illinois, of any other state, or of any political subdivision or agency of the State of Illinois or of any other state, whether the interest earned thereon is taxable or tax-exempt under federal law. The bonds shall be rated at the time of purchase within the four highest general classifications established by a rating service of nationally recognized expertise in rating bonds of states and their political subdivisions.

2. *Collateralization*

Acceptable collateral securities must be such securities as are authorized securities for investment by the District as further limited and defined from time to time by the Treasurer. Certain secure letters of credit can be acceptable collateral as determined by the Treasurer.

Investment in certificates of deposit or time deposits will be collateralized with permitted securities of the U.S. Government or Irrevocable Letters of Credit issued by the Federal Home Loan Bank (FHLB) at 105% or 102% of market value, respectively, of the monies on deposit excluding the amount insured by the FDIC. Such collateral will be marked to market on a semi-monthly basis to determine adequacy of value. Any shortfall requires deposit of the necessary value of additional collateral securities as quickly as possible.

Repurchase agreements shall be done using only direct U.S. Treasury securities as the investment asset. The securities must be maintained at a value of at least 102% of the District investment amount at market value.

All investment collateral will be held in safekeeping by a third party custodial institution as designated by the Treasurer, in the District's name, and maintained at the required levels for the investment type.

Banks holding operating bank accounts of the District are required to provide permitted securities of the U.S. Government as collateral against such account balances equal to 105% of market value of the monies on deposit, excluding the amount insured by the FDIC.

VI. Investment Parameters

1. *Diversification*

The investments shall be diversified by:

a. limiting investments to avoid overconcentration in securities from a specific issuer or business sector (excluding U.S. Treasury securities) by incorporating the following guidelines:

    i. Commercial paper held may not exceed one-third (33%) of the District's portfolio.

    ii. Generally no more than twenty percent (20%) of funds invested in commercial paper may be in the paper of any one entity. In situations where the District determines divestiture of this asset class is necessary to protect the valuation, safety or liquidity of the portfolio, the holding of some securities through maturity may be deemed the prudent action. In such a case, the amount in the portfolio may temporarily exceed the 20% limit until remaining securities mature.

iii. Certificates of Deposit – The District shall at no time hold certificates of deposit constituting more than ten percent (10%) of the total deposits of the issuing institution.

b. Due to inherent difficulties in accurately forecasting cash flow, a portion of the portfolio in readily available money market funds such as the State Treasurers' Illinois Funds, interest-bearing savings accounts, overnight repurchase agreements, or commercial paper to ensure that appropriate liquidity is maintained in order to meet ongoing daily obligations.

2. *Maximum Maturities*

To the greatest extent possible, the District shall attempt to match its investment maturities to anticipated cash flow requirements. Unless matched to a specific cash flow, the District will not directly invest in securities maturing more than five (5) years from the date of purchase.

Any intent to invest in securities with maturities exceeding five (5) years from the date of purchase shall be disclosed in writing to the Board of Commissioners of the District.

3. *Pooling of Funds*

Except for cash in any restricted or special Funds, the District may consolidate available cash balances from the various Funds in joint investment when advantageous, in order to maximize investment earnings. In such investment, investment income earned will be allocated to the various participating Funds based on the investment amount percentage of each fund to total investment.

VII. Reporting and Performance Measures

1. *Reports*

a. Reports Required by Statute – The Treasurer shall prepare for the Board of Commissioners a monthly report of investment interest income by major fund, detail of investments purchased by fund, and any other reports as may from time to time be required under the statutes and presented as agenda items at regularly scheduled Board Meetings.

b. Preparation of Other Reports – The Treasurer shall provide to the Board of Commissioners any such other reports of Treasury activities as the Board may request.

2. *Performance Standards*

The investment portfolio will be managed in accordance with the parameters specified within this policy. The portfolio should obtain a market average rate of return for like maturity horizons during a market/economic environment of stable interest rates. The ending quarterly investment inventory should bear an average interest rate comparable to or higher than the 90-day Treasury bill rate for the end of that quarter.

3. *Marking to Market*

The market value of the portfolio shall be calculated at least quarterly and a statement of the market value of the portfolio shall be issued at least quarterly. This will ensure that review of the investment portfolio, in terms of value and price volatility, has been performed consistent with the GFOA Recommended Practice on "Mark-to-Market Practices for State and Local Government Investment Portfolios and Investment Pools." In defining market value, considerations should be given to the GASB Statement 31 pronouncement.

VIII. Policy Considerations

1. *Exemption*

Any investment held at time of passage of this policy that does not meet the guidelines of this policy shall be exempted from the requirements of this policy. At maturity or liquidation, such monies shall be reinvested only as provided for in this policy.

2. *Amendments*

This policy shall be amended as and when deemed necessary. Any changes initiated must be approved by the Treasurer and the Board of Commissioners.