VILLAGE OF BANNOCKBURN INVESTMENT POLICY

§28-1. Investment Policy

A. GLOSSARY OF TERMS

(1) Accrued Interest – The accumulated interest due on a bond as of the last interest payment made by the issuer.

(2) Agency: A debt security issued by a federal or federally sponsored agency. Federal agencies are backed by the full faith and credit of the U. S. Government. Federally sponsored agencies (FSAs) are backed by each particular agency with a market perception that there is an implicit Government guarantee. An example of a Federal agency is the Government National Mortgage Association (GNMA). An example of a FSA is the Federal National Mortgage Association (FNMA).

(3) Amortization: The process of paying the principal amount of an issue of bonds by periodic payments either directly to bondholders or to a sinking fund for the benefit of bondholders.

(4) Arbitrage: Usually refers to the difference between the interest paid on the tax-exempt securities and the interest earned by investing the proceeds in higher yielding taxable securities. Internal Revenue Service regulations govern arbitrage (reference I.R.S. Reg. 1.103-13 through 1.103-15).

(5) Arbitrage Bonds: Bonds which are deemed by the I.R.S. to violate federal arbitrage regulations. The interest on such bonds becomes taxable and the bondholders must include this interest as part of gross income for federal income tax purposes (I.R.S. Reg. 1.103-13 through 1.103-15).

(6) Asked: The price at which securities are offered.

(7) Assessed Value: An annual determination of the just or fair market value of property for purposes of ad valorem taxation.

(8) Average Life: The average length of time that issues of serial bonds and/or term bonds with a mandatory sinking fund feature is expected to be outstanding.

(9) Bankers' Acceptance (BA): A draft or bill or exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the issuer.

(10) Basis Point: 1/100 of one percent.

(11) Bid: The indicated price at which a buyer is willing to purchase a security or commodity. Bond - Written evidence of the issuer's obligation to repay a specified principal amount on a date certain, together with interest at a stated rate, or according to a formula for determining that rate.

(12) Bond Anticipation Notes (BANS) - Short-term interest bearing notes issued by a government in anticipation of bonds to be issued at a later date. The notes are retired from proceeds of the bond issue to which they are related.

(13) Broker: A broker brings buyers and sellers together for a commission paid by the initiator of the transaction or by both sides; he does not position (take ownership of securities). In the money market, brokers are active in markets in which banks buy and sell money in interdealer markets.

(14) Callable Bond: A bond which permits or requires the issuer to redeem the obligation before the stated maturity date at a specified price, the call price, usually at or above par value.

(15) Cash Sale/Purchase: A transaction which calls for delivery and payment of securities on the same day that the transaction is initiated.

(16) Certificate of Deposit (CD): A time deposit with a specific maturity evidenced by a certificate.

(17) Collateralization: Process by which a borrower pledges securities, property, or other deposits for the purpose of securing the repayment of a loan and/or security. Also, refers to securities pledged by a bank to secure deposits of public monies.

(18) Commercial Paper: Very short-term, unsecured promissory notes issued in either registered or bearer form, and usually backed by a line of credit with a bank.

(19) Comprehensive Annual Financial Report (CAFR): The official annual report for the Village of Bannockburn. In addition to a combined, combining (assembling of data for all funds within a type), and individual balance sheet, the following are also presented as appropriate on a combined, combining, and individual basis: (1) statement of revenues, expenditures, and changes in fund balance (all funds); (2) statement of revenues, expenditures, and changes in fund balances, budget and actual (for government fund types); (3) statement of revenues, expenses, and changes in retained earnings (for proprietary funds); and (4) statement of changes in financial position (for proprietary funds).

(20) Convexity: A measure of a bond's price sensitivity to changing interest rates. A high convexity indicates greater sensitivity of a bond's price to interest rate changes.

(21) Coupon:
a. The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value.
b. A certificate attached to a bond evidencing interest due on a payment date.

(22) Coupon Rate: The annual rate of interest payable on a coupon bond (a bearer bond or bond registered as to principal only, carrying coupons evidencing future interest payments), expressed as a percentage of the principal amount.

(23) Credit Risk: The risk to an investor that an issuer will default in the payment of interest and/or principal on a security.

(24) Current Yield (Current Return): A yield calculation determined by dividing the annual interest received on a security by the current market price of that security.

(25) Dealer: A dealer, as opposed to a broker, acts as a principal in all transactions, buying and selling securities from an inventory on hand.

(26) Debenture: A bond secured only by the general credit of the issuer. When the Village issues bonds of this they are termed General Obligation (G.O).

(27) Delivery versus Payment: There are two methods of delivery of securities: delivery versus payment and delivery versus receipt (also called free). Delivery versus payment is delivery of securities with an exchange of money for the securities. Delivery versus receipt is delivery of securities with an exchange of signed receipt for the securities.

(28) Derivative Security: Financial instrument created from, or whose value depends upon, one or more underlying assets or indexes of asset values.

(29) Discount: The amount by which the par value of a security exceeds the price paid for the security.

(30) Discount Securities: Non-interest bearing money market instruments that are issued at a discount and redeemed at maturity for full face value: e.g. U.S. Treasury Bills, Zero Coupon Bonds.

(31) Diversification – A process of investing assets among a range of security types by sector, maturity, and quality rating. The purpose of diversification is to minimize risk from default or market fluctuations.

(32) Duration: A measure of the timing of the cash flows, such as the interest payments and the principal repayment, to be received from a given fixed income security. This calculation is based on three variables; term to maturity, coupon rate and yield to maturity. The duration of a security is a useful indicator of its price volatility for given changes in interest rates.

(33) **Enterprise Funds**: Funds that are financed and operated in a manner similar to private business in that goods and services provided are financed primarily through user charges.

(34) **Federal Credit Agencies:** Agencies of the Federal government set up to supply credit to various classes of institutions and individuals; e.g. S&L's, small business firms, students, farmers, farm cooperatives, and exporters.

(35) **Federal Deposit Insurance Corporation:** A Federal Agency that insures deposits and retirement accounts in member accounts for up to $250,000, protecting depositors in the event of bank failure.

(36) **Federal Funds (Fed Funds)**: Funds placed in Federal Reserve banks by depository institutions in excess of current reserve requirements. These depository institutions may lend to Fed Funds to each other overnight or on a longer basis. They may also transfer funds among each other on a same-day basis through the Federal Reserve banking system. Fed funds are considered to be immediately available funds.

(37) **Federal Funds Rate:** Interest rate charged by one institution lending federal funds to the other.

(38) **Federal Home Loan Bank:** FHLB system now primarily focuses on increasing the amount of loanable funds available for affordable housing and community development projects. It continues to have a material impact on housing and development financing, offering funds to member institutions at rates that are usually lower than commercially competitive prices.

(39) **Federal National Mortgage Association:** FNMA, commonly known as Fannie Mae, is a government-sponsored enterprise that is the largest purchaser and guarantor of home mortgages in the country. Headquartered in Washington, D.C., Fannie Mae buys mortgages from such lenders as banks and savings and loans, packages them, and resells them on the open market, thus creating fluidity and lessening lenders' risk. Fannie Mae's creation of this secondary mortgage market enables low- and middle-income individuals and families to obtain mortgages and purchase homes. The corporation was founded (1938) by the federal government to buy and sell mortgages insured by the Federal Housing Administration or guaranteed by the Veterans Administration (now the Veterans Affairs Dept.).

(40) **Federal Reserve System:** The seven-member Board of Governors of the Federal Reserve System determines the reserve requirements of the member banks within statutory limits, reviews and determines the discount rates established by the 12 Federal Reserve banks, with each one serving member banks in its own district. This system, supervised by the Federal Reserve Board, has broad regulatory powers over the money supply and the credit structure.

(41) **Government National Mortgage Association:** (GNMA), or Ginnie Mae, which is administered by the Dept. of Housing and Urban Development and helps to finance public housing. Fannie Mae's corporate credibility was damaged by revelations (2004) that it manipulated its earnings from 1998 to 2004, in part to maximize bonus payments to its corporate executives. Problems in the housing and mortgage industry that began in 2007 led in 2008 to increasing losses at and concern about a possible bankruptcy of Fannie Mae and especially Freddie Mac (the Federal Home Loan Mortgage Corporation), and resulted in a federal takeover of the two mortgage guarantors.

(42) **Government Securities:** An obligation of the U.S. government, backed by the full faith and credit of the government. These securities are regarded as the highest quality of investment securities available in the U.S. securities market.

(43) **Interest Rate**: See "Coupon Rate."

(44) **Interest Rate Risk**: The risk associated with declines or rises in interest rates which cause an investment in a fixed – income security to increase or decrease in value.

(45) **Liquidity**: An asset that can be converted easily and quickly into cash.

(46) **Local Government Investment Pool** (LGIP): An investment by local governments in which their money is pooled as a method for managing local funds.

(47) **Market-to-Market**: The process whereby the book value or collateral value of a security is adjusted to reflect its current market value.

(48) **Market Risk:** The risk that the value of a security will rise or decline as a result of changes in market conditions.

(49) **Market Value:** Current market price of a security.

(50) **Maturity**: The date upon which the principal of a municipal bond becomes due and payable to bondholders.

(51) **Net Asset Value:** The market value of one share of an investment company, such as a mutual fund. This figure is calculated by totaling a fund's assets which includes securities, cash, and any accrued earnings, subtracting this from the fund's liabilities, and dividing this total by the number of shares outstanding.

(52) **Net Interest Cost (NIC)**: The traditional method of calculating bids for new issues of municipal securities. The total dollar amount of interest over the life of the bonds is adjusted by the amount of premium or discount bid, and then reduced to an average annual rate. The other method is known as the true interest cost (see "true interest cost").

(53) **Par Value or Face Amount:** In the case of bonds, the amount of principal which must be paid at maturity.

(54) **Principal:** The face amount or par value of a bond or issue of bonds payable on stated dates of maturity.

(55) **Prudent Person Rule:** An investment standard outlining the fiduciary responsibilities of public funds investors relating to investment practices.

(56) **Ratings:** Evaluations of the credit quality of notes and bonds, usually made by independent rating services, which generally measure the probability of the timely repayment of principal and interest on municipal bonds.

(57) **Repurchase Agreement** (RP or REPO): An agreement of one party to sell securities at a specified price to a second party and a simultaneous agreement of the first party to repurchase the securities at a specified price or at a specified later date. The security "buyer" in effect lends the "seller" money for the period of the agreement, and terms of the agreement are structures to compensate him. Dealers use RP extensively to finance their positions. Exception: When the Fed is said to be doing RP, it is lending money; this is, increasing bank reserves.

(58) **Safekeeping**: A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank's vaults for protection.

(59) **SEC RULE 15C3-1**: See definition of Uniform Net Capital Rule in this subsection.

(60) **Secondary Market:** A market made for the purchase and sale of outstanding issues following the initial distribution.

(61) **Securities and Exchange Commission:** Federal agency created by the securities exchange act of 1934 to administer that act and the securities act of 1933, formerly carried out by the federal trade commission. The SEC supervises the exchange of securities so as to protect investors against malpractice.

(62) **Short-Term Debt**: Short-term debt is defined as any debt incurred whose final maturity is three years or less.

(63) **Swap**: Trading one asset for another.

(64) **Term Bonds:** Bonds coming due in a single maturity.

(65) **Total Return:** The sum of all investment income plus changes in the capital value of the portfolio.

(66) **Treasury Bills:** A short-term obligation of the U.S. Treasury having a maturity period of one year or less and sold at a discount from face value. The return to the investor who holds it to maturity is the difference between the price paid and the face value at maturity.

(67) Treasury Bond: A long-term obligation of the U.S. Treasury having a maturity period of more than ten years and paying interest semiannually.

(68) Treasury Notes: An intermediate-term obligation of the U.S. Treasury having a maturity period of one to ten years and paying interest semiannually.

(69) Uniform Net Capital Rule (Net Capital Rule and Net Capital Ratio): Securities and Exchange Commission requirement that member firms as well as non-member broker/dealers in securities maintain a maximum ratio of indebtedness to liquid capital of 15 to 1. Indebtedness covers all money owed to a firm, including margin loans and commitments to purchase securities, one reason new public issues are spread among members of underwriting syndicates. Liquid capital includes cash and assets easily converted into cash.

(70) Volatility: A degree of fluctuation in the price and valuation of securities.

(71) Weighted Average Maturity (WAM): – The average maturity of all the securities that comprise a portfolio.

(72) Yield: The current rate of return on an investment security generally expressed as a percentage of the security's current price. (a) **Income Yield** is obtained by dividing the current dollar income by the current market price for the security, (b) **Net Yield or Yield to Maturity** is the current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond.

(73) Yield to Maturity: The rate of return to the investor earned from payments of principal and interest, with interest compounded semiannually and assuming that interest paid is reinvested at the same rate.

(74) Zero Coupon Bond: A bond which pays no interest, but is issued at a deep discount from par, appreciating to its full value at maturity.

B. POLICY

The intent of the Investment Policy of the Village of Bannockburn is to define the policies for maximizing the efficiency of the Village's Cash Management System and for prudent investment of the Village's Funds, and to provide guidelines for suitable investments.

The ultimate goal is to enhance the economic status of the Village while protecting its funds.

The Village's Cash Management System is designed to monitor and forecast expenditures and revenues accurately, thus enabling the Village Board (through the Village Manager, Finance Commissioner, and Finance Director) to invest funds to the fullest extent possible. The Village Manager, Finance Commissioner, and Finance Director shall attempt to obtain the highest investment return using authorized instruments that meet the criteria established for safety and liquidity while meeting the Village's daily cash flow demands in conformance with the Municipal Code.

The investment policies and practices of the Village of Bannockburn are based upon Federal, State, and Local law and prudent money management. The Policy has been prepared in accordance with the Public Funds Investment Act (30 ILCS 235 / 2.5). The primary goals of these policies are:

1. To assure compliance with all Federal, State and Local laws governing the investment of monies under the control of the Village.
2. To protect the principal monies of the Village, and
3. To generate the maximum amount of investment income within the parameters of this Investment Policy and the guidelines for suitable investments.

All participants in the Village's investment process [including without limitation the Village Manager, Finance Commissioner, and Finance Director the "Investment Officials")] shall act responsibly as custodians of the public trust. Investment Officials shall recognize that the investment portfolio is subject to public review and evaluation. The overall program shall be designed and managed with a degree of professionalism that is worthy of the public trust.

C. SCOPE

This investment policy applies to the investment of available assets of all Village funds under the direct management of the Village Board of Trustees and Investment Officials.

The policy for the Illinois Municipal Retirement Fund (IMRF) will be as determined by the appropriate Boards of Administration and not covered by this Policy.

Funds set aside to decrease Village debt in conjunction with an advance refunding agreement will be invested in accordance with appropriate bond documents.

Should bond covenants be more restrictive than this policy, funds will be invested in full compliance with those restrictions.

Funds held by the County Treasurer during tax collection periods shall be governed by the County's investment policies to the extent that they do not conflict with this policy and should be invested by the County Treasurer for the benefit of the Village of Bannockburn as stipulated by the Village in accordance with 55 ILCS 5/3-11006.

All investments of the Village of Bannockburn must be made in compliance with applicable Federal and State law and in accordance with applicable legal interpretations. Investment of any tax-exempt borrowing proceeds and of any debt service funds must comply with the 1986 Tax Reform Act if the act applies to the debt issued.

D. PRUDENCE

Investments shall be made with judgment and care under circumstances then prevailing-that 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.

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. Investment Officials acting in accordance with written procedures and the 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 appropriate action is taken to control adverse developments.

The Board recognizes that that material, relevant, and decision-useful sustainability factors have been or are regularly considered by the Board, within the bounds of financial and fiduciary prudence, in evaluating investment decisions. Such factors include, but are not limited to: (1) corporate governance and leadership factors; (2) environmental factors; (3) social capital factors; (4) human capital factors; and (5) business model and innovation factors, as provided under the Illinois Sustainable Investing Act. (40 ILCS 5/1-113.6 and 1-113.17)

E. OBJECTIVE

The primary objective in the investment of Village funds under control of the Village Board of Trustees and Investment Officials is to ensure the safety of principal, while managing liquidity requirements of debt service and other financial obligations of the Village and providing the highest investment return using authorized investment instruments.

The primary objectives of the Village of Bannockburn investment activities are as follows:

> Legality: The Village's investments will be in compliance with all statutes governing the investment of public funds.
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> Safety: Investments of the Village will be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. To attain this objective, diversification is required in order that the Village Investment Officials prudently manages market interest rate and credit risk.
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> Liquidity: The Village's investments will remain sufficiently liquid to enable the Village to meet all operating requirements that might be reasonably anticipated.

Return on Investments/Yield: The Village's investment portfolio shall be designed to obtain the highest available return, taking into account the Village's investment risk constraints and cash flow needs. The Investment Officials shall seek to obtain the highest available return using authorized investments.

F. ETHICS AND CONFLICT OF INTEREST

It is the policy of the Village that no person acting on behalf of the investment function shall, in any manner, have any interest, either directly or indirectly, in any investments in which the Village is authorized to invest, or receive in any manner, compensation of any kind, from any investments from the sellers, sponsors, or managers of such investments. All persons authorized to trade on behalf of the Village must refrain from personal business activity that could potentially conflict with proper execution of this Investment Policy or impair their ability to make impartial decisions.

Investment advisors and money managers must adhere to a minimum level of standards consistent with the Association for Investment Management and Research Code of Ethics. If a more stringent regulation applies under an advisor's or manager's certification standard, than this policy dictates as the ethical benchmark.

G. DELEGATION OF AUTHORITY

Management responsibility for the investment program is hereby delegated to the Investment Officials who shall establish written procedures for the operation of the investment program consistent with this investment policy and approved by the Village Board (the "Investment Procedures"). Such procedures shall include explicit delegation of authority to persons responsible for investment transactions. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the Investment Officials and approved by the Village Board. The Finance Commissioner shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate Investment Officials.

H. AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS

The Village Investment Officials will maintain a list of financial institutions authorized to provide investment services in the Village. The selection process for inclusion on this list will be detailed in the written administrative procedures for investments. No public deposits shall be made except in municipal depositories approved by the Village Board.

Depositories: The Village has allowed only regularly organized state or national banks insured by the Federal Deposit Insurance Corporation ("FDIC") and federal and state savings and loan associations insured by Savings Association Insurance Fund of the FDIC to be designed as possible municipal depositories. Depository institutions should be economically viable and have practices that would not impair the safety of investments.

Broker/Dealer: The Village Investment Officials shall evaluate interested broker/dealers on the basis of criteria set by the Village Investment Officials, including the firm's prior experience, financial stability, and other requirements deemed necessary. All financial institutions and broker/dealers who desire to become qualified bidders for investment transactions must supply the Finance Director with the following: audited financial statements, proof of National Association of Security Dealers certification, proof of State registration. An annual review of the financial condition and registrations of qualified bidders will be conducted by the Finance Director.

Authorized Advisors/Money Managers: This policy requires that investment advisors possess the following qualifications:

1. Minimum five (5) years' continuous service for municipal clients.
2. Minimum three (3) years' municipal clients as current references.
3. Minimum licensing and certification as accepted in the industry for the service engaged.

I. AUTHORIZED INVESTMENTS

The Village of Bannockburn is empowered to invest in certain types of securities as detailed in the Public Funds Act 30 ILCS 235. Among the authorized investments are:

1. 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;
2. U.S. agency and instrumental obligations which are limited to the following issuers:

   a. Federal Home Loan Bank (FHLB)
   b. Federal Home Loan Mortgage Corporation (FHLMC)
   c. Federal Farm Credit Bank (FFCB)
   d. Government National Mortgage Association (GNMA)
   e. Federal Agricultural Mortgage Corporation (FarmerMac)
   f. Tennessee Valley Authority (TVA)
   g. Federal National Mortgage Association (FNMA)
   h. Any other agency created by an Act of Congress
3. Institutional size depository investments such as 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, including bankers' acceptance and bank notes.
   a. The instruments or issuers shall have short-term ratings in one of the highest 2 classifications without regard to gradation by at least two rating agencies, one of which must be Standard and Poor's ("S&P") or Moody's, and long-term rating in one of the highest 3 classifications without regard to gradation by at least two rating agencies, one of which must be S&P or Moody's.
   b. Investments may be made only in banks which are insured by the Federal Deposit Insurance Corporation. Any amount of the deposit in excess of the federal deposit insurance shall be either: (1) fully collateralized at least 105% percent by: (i) marketable U.S. government securities marked to market at least monthly; (ii) bonds, notes, or other securities constituting the direct and general obligation of any agency or instrumentality of the United States; or (iii) bonds, notes or other securities constituting a direct and general obligation of any county, township, Village, village, incorporated town, municipal corporation, or school district, of the State of Illinois or of any other state, or of any political subdivision or agency of the State of Illinois or any other state which are rated in either the AAA or AA rating categories by at least two accredited ratings agencies and maintaining such rating during the term of such investments; or (2) secured by a corporate surety bond issued by an insurance company licensed to do business in Illinois and having a claims-paying rating in the top rating category as rated by a nationally recognized statistical rating organization and maintaining such rating during the term of such investment;
4. Short term obligations of corporations organized in the United States with assets exceeding $500,000,000 if (i) such obligations are rated at the time of purchase in either the AAA or AA rating categories by at least 2 standard rating services and which mature not later than 180 days from the date of purchase, (ii) such purchases do not exceed 10% of the corporation's outstanding obligations and (iii) no more than 5% of the public agency's funds may be invested in short term obligations of corporations; or
5. 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 paragraph (1) or (2) of this subsection and to agreements to repurchase such obligations and that such fund has a short-term rating of "AAAm" by S&P or Aaa by Moody's.
6. Interest bearing bonds of any county, township, Village, village, incorporated town, municipal corporation, or school district. The bonds shall be registered in the name of the Village or held under a custodial agreement at a bank. The bonds shall be rated at the time of purchase within the 4 highest general classifications established by at least two accredited rating agencies of nationally recognized expertise in rating bonds of states and their political subdivisions.
7. Bond funds registered under the Investment Company Act of 1940, as amended from time to time, provided that the portfolio is limited to bonds, notes, treasury bills, or other securities which are guaranteed by the United States government or agreements to repurchase these same types of obligations, and qualified U.S. agencies under 30 ILCS 235 et. seq.
8. Public Treasurers' Investment Pool created under Section 17 of the State Treasurer Act with a short-term rating of "AAAm" by S&P.
9. Repurchase agreements pursuant to the Investment Act. The securities, unless registered or inscribed in the name of the Village, shall be purchased through banks or trust companies authorized to do business in the State of Illinois. The term "repurchase agreements" as used herein shall include flexible repurchase agreements that permit the Village to withdraw funds as needed and master repurchase agreements that permit the deposit, withdrawal and redeposit of funds over time.

   The securities described in clauses (1) and (2) above, or any other securities that the Village is authorized to acquire under law, may be acquired pursuant to agreements entered into between the Village and suppliers of such securities under which agreements suppliers agree to sell to the Village specified securities on specific dates at specific prices, all as established at the time of execution and delivery of any such agreements and as set forth in such agreements.

J. INVESTMENT RESTRICTIONS

The Village Investment Officials will not utilize investment of leveraged transactions, financial forwards, futures, hedged investments, index amortizing notes, dual index notes, de-leveraged bonds, range bonds, inverse floaters, interest only, principal only bonds and any other financial derivative. The Village Investment Officials are not authorized, without the approval of the Village Board, to (i) invest in financial agreements whose returns are linked to or derived from the performance of some underlying asset such as bonds, currencies or commodities products, or (ii) borrow against or otherwise obligate Village investments.

K. **COLLATERALIZATION**

In order to protect the Village public funds deposits, collateralization shall be required on all deposits, certificates of deposits, investments and repurchase agreements. So as to anticipate market changes and provide an adequate level of security for all funds, the collateralization level will be at least 105% of market value of principal and accrued interest. Collateral is required as security for any amount in excess of the federal deposit insurance limit. Collateral is limited to government or approved securities or surety bonds issued by top-rated insurers.

Collateral will always be held by an independent third party with whom the entity has a current custodial agreement. A clearly marked evidence of ownership (safekeeping receipt) must be supplied to the entity and retained. The bank will provide the Village a copy of the Board minutes that approved the collateralization. Each time collateral is changed it must be approved by the Village. The change must be recorded in the next Bank Board Minutes and a copy of the minutes must be furnished to the Village.

L. SAFEKEEPING AND CUSTODY

To protect against potential fraud, embezzlement, or losses caused by collapse of individual securities dealers, all investment securities purchased by the Village, including collateral on repurchase agreements, shall be held by the Village or in safekeeping by the Village's custodian bank or a third party bank trust department, acting as agent for the Village under the terms of a custody or trustee agreement executed by the bank and by the Village. The primary agent shall issue a safekeeping receipt to the Village listing the specific instrument, rate, maturity, and other pertinent information.

All securities transactions conducted by the custodian on behalf of the Village are to be on a delivery-versus payment (DVP) only basis.

Investment officials shall be bonded to protect the Village against loss due to possible embezzlement and malfeasance.

M. DIVERSIFICATION

A variety of financial instruments and maturities, properly balanced, will help to ensure liquidity and reduce risk or interest rate volatility and loss of principal. Diversifying investments and maturities will avoid incurring unreasonable risks in the investment portfolio regarding specific security types, issuers or individual financial institutions. With the exception of U.S. Treasury securities and authorized pools, no more than 50% of the Village's total investment portfolio will be instead in a single security type or with a single financial institution.

N. MATURITIES

To the extent possible, the Village will attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the Village will not directly invest in securities maturing more than three (3) years from the date of purchase. However, the Village may collateralize its repurchase agreements using longer-dated investment.

Reserve or Capital Improvement Project monies may be invested in securities not to exceed three (3) years. The maturity of such investments is made to coincide as nearly as possible with the expected use of the funds.

O. RISK MANAGEMENT

Market Risk, Credit Risk, and Liquidity Risk, are typically associated with fixed income portfolio management. Their definition and the techniques used to control, evaluate and manage them are also discussed below:

1. Market Risk - the risk that the value of a security will rise or decline as a result of changes in market conditions.
    a. Control Technique - the Village Investment Officials shall provide for market to market valuations on a monthly basis.
2. Credit Risk - the risk that an issuer will default in the payment of interest and/or principal on a security.
    a. Control Technique - the Village Investment Officials will limit investments to the safest types of securities, pre-qualify the financial institutions, broker/dealers, intermediaries and advisers with which the Village will do business, and diversify the investment portfolio so that potential losses on individual securities will be minimized. The Finance Director shall provide ongoing evaluation and monitoring of creditworthiness of all counterparties.
3. Liquidity Risk - the risk that an asset cannot be converted quickly and easily into cash.
    a. Control Technique - the Village Investment Officials shall create and maintain cash flow forecasts and will select securities and maturities that meet cash flow needs and provide for diversification within the portfolio to ensure compliance with established policy limits.

In addition to the aforementioned control techniques, any investment manager who is retained to manage assets on behalf of the Village is also required to participate in the risk management process and adhere to the Village's Investment Policy.

P. INTERNAL CONTROLS

The Village Investment Officials shall maintain a system of internal controls and written operational procedures that shall be documented. The Village is subject to annual independent review of its internal controls by an independent accounting firm. This review will provide assurance that policies and procedures are being complied with. Such review also may result in recommendations to change operating procedures to improve internal control. The controls shall be designed to prevent loss of public funds due to fraud, error, misrepresentation by third parties, unanticipated market changes, or imprudent actions by employees or officers of the Village.

In addition, the Village Investment Officials have established a system of internal controls to ensure that staff positions and functional duties are adequately segregated for separation of duties between investment and accounting operations.

Q. PERFORMANCE STANDARDS

The Village's investment portfolio will be designed to obtain a market average rate of return during budgetary and economic cycles, taking into account the Village's investment risk constraints and cash flow needs.

The Village's Finance Director will utilize the average three-month Treasury Bill return or other appropriate benchmarks to determine whether average yields are being achieved.

R. ACCOUNTING

All investment transactions shall be recorded in the various Village Funds in accordance with generally accepted accounting principles as promulgated by the Government Accounting Standards Board.

S. REPORTING

The Village's Finance Director shall submit quarterly an investment report to the Village Board that summarizes recent market conditions, economic developments and anticipated investment conditions. The report shall summarize the investment strategies employed in the most recent quarter, description of the portfolio in terms of investment securities, maturities, risk characteristics and other features. The report shall explain the quarter's total investment return and compare the return with target rate of return projections and budgetary expectations.

T. CORRECTION OF NONCOMPLIANCE

In the event of changes in market, the Investment Act or other applicable law, current holdings could fail to meet the guidelines of this policy. Whenever that occurs, the Village's Finance Director will immediately notify the Village Manager, and appropriate action will be taken.

U. INVESTMENT POLICY ADOPTION

The Village's investment policy as adopted by ordinance of the Village Board shall be reviewed annually by the Investment Officials and any recommended modifications thereto must be approved by the Village Board.

This policy supersedes all prior investment policies.