

METROPOLITAN ST. LOUIS SEWER DISTRICT

PUBLIC FUNDS INVESTMENT POLICY

-Adopted February 8, 2001

METROPOLITAN ST. LOUIS SEWER DISTRICT
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I. PURPOSE

The purpose of this Public Funds Investment Policy (this "Policy") is to outline the standards applicable to the investment of public funds of the Metropolitan St. Louis Sewer District (the "District") and to describe the investments permitted.

II. SCOPE OF INVESTMENT POLICY

The Policy applies to all financial assets of the District as accounted for in the District's Secretary-Treasurer's Monthly Report. These funds include:

- Construction Escrow Fund;
- Clean Water Capital Improvement Fund;
- Mississippi River Bond Fund; and
- Pooled Investments Fund

Except for cash in certain restricted and special funds, the District will consolidate cash balances from all funds to obtain economies of scale. Investment income will be allocated to various funds based on their respective participation and in accordance with generally accepted accounting principals.

This section does not apply to the District's pension funds. Any new fund created by the District's Board of Trustees (the "Board"), unless specifically exempted by the Board or by law, shall be presumed to be within the scope of this section.

Investment through external programs, facilities and professionals operating in a manner consistent with this Policy will constitute compliance.

III. OBJECTIVES

Subject to the legal restrictions on investments imposed by the Missouri Constitution, Missouri State Statute and the Plan of the Metropolitan St. Louis Sewer District, as amended (the "Plan") and District Ordinances, the District's primary objectives in its investment activities, **in order of priority**, shall be:

First – SAFETY: Preservation of principal is the foremost objective of the District's investment program. Investments of the District 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 and interest rate risk.

a. Credit Risk

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

- 1) Pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisors with which the District will do business; and
- 2) Diversifying the portfolio so that potential losses on individual securities will be minimized.

b. Interest Rate Risk

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

- 1) Structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity; and
- 2) Investing operating funds primarily in short-term securities.

Second - LIQUIDITY: The District's investment portfolio shall remain sufficiently liquid to meet all operating and debt service obligations that may be reasonably anticipated. This is accomplished by structuring the portfolio so that the securities mature with cash needs to meet anticipated demands. Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets. A portion of the portfolio also may be placed in bank deposits or repurchase agreements that offer same-day or next-day liquidity for short-term funds.

Third – YIELD: The District's investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the Safety and Liquidity objectives stated above. Return on investment is of secondary importance compared to the Safety and Liquidity objectives described above. The core of investments are limited to relatively low risk securities in anticipation of earning a fair return relative to the risk assumed. Securities shall not be sold prior to maturity except when:

- 1) Sale of a security with declining credit may minimize the risk of loss of principal;
- 2) A security swap would improve the quality, yield, or target duration in the portfolio; or
- 3) Liquidity needs of the portfolio require that the security be sold.

Fourth – LOCAL ECONOMIC BENEFIT: While satisfying the objectives of Safety, Liquidity and Yield, the District shall seek to place investments with financial institutions that demonstrate a strong record of investing in, and supporting the local economy through the institutions' lending practices.

Fifth – SOCIAL POLICY: While satisfying the objectives of Safety, Liquidity and Yield, investment decisions should further the District's social policies established by the District's Board.

IV. STANDARD OF CARE

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. Under the prudent person standard, investments shall be made with judgment and care, under the 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. Investment officers acting in accordance with written procedures and this 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.

V. ETHICS AND CONFLICTS OF INTEREST

Officers and employees involved in the investment process shall refrain from 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. Employees and investment officials shall disclose any material interests in financial institutions with which they conduct business. They shall further disclose any personal financial or investment positions that could be related to the performance of the investment portfolio. Employees and officers shall refrain from undertaking personal investment transactions with individuals with whom business is conducted on behalf of the District.

VI. DELEGATION AND SCOPE OF AUTHORITY

Authority to manage the investment program of the District is granted to the Secretary Treasurer, with approval of the Board, as derived from Section 7.020 of the Plan. The Secretary-Treasurer shall act in accordance with the established written procedures and internal controls for the operation of the investment program consistent with this Policy. Procedures should include references to: safekeeping, delivery vs. payment, investing and 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 Board. The Secretary-Treasurer shall be responsible for all transactions undertaken and shall establish procedures to regulate the activities of subordinate officials.

VII. INTERNAL CONTROLS

The Secretary-Treasurer shall establish a system of internal controls designed to ensure that the assets of the District are protected from loss, theft or misuse. The internal controls shall be designed to provide reasonable assurance that these objectives are met. Reasonable assurance recognizes that (1) the cost of a control should not exceed the anticipated benefits likely to be derived and (2) the valuation of costs and benefits requires estimates and judgments by the Secretary-Treasurer. Accordingly, the Secretary-Treasurer shall establish a process for annual independent review by an external auditor to assure compliance with this Policy and the procedures set by the Secretary-Treasurer.

The internal controls shall address the following:

- a. Control of collusion;
- b. Separation of transaction authority from accounting and record keeping;
- c. Custodial safekeeping;
- d. Avoidance of bearer or physical delivery securities;
- e. Clear delegation of authority to staff members;
- f. Written confirmation of telephone transactions; and
- g. Development of a wire transfer agreement with the lead bank and third party custodian.

VIII. SUITABLE AND AUTHORIZED INVESTMENTS

Consistent with the Plan, the following investments will be permitted by this Policy:

- a. Obligations of the United States Government;
- b. Obligations of any agency or instrumentality of the United States;
- c. Time certificates of deposit secured by collateral as required by statute and in the section "Collateralization" of this Policy;
- d. Repurchase agreements maturing and payable within 90 days and secured by collateral as required by statute and in the section "Collateralization" of this Policy;

- e. Deposits with "Approved Depository Banks" (defined below), provided the Approved Depository Banks shall give a bond equal to the deposit, with good and sufficient sureties, or the deposit of collateral as required by statute and in the section "Collateralization" of this Policy;
- f. Banker's Acceptances issued by domestic commercial banks possessing the highest rating issued by a nationally recognized rating agency and maturing and becoming payable not more than one hundred eighty days from the date of purchase; and
- g. Commercial paper issued by domestic corporations which has received the highest rating issued by a nationally recognized rating agency and maturing and becoming payable not more than one hundred eighty days from the date of purchase. Eligible commercial paper is further limited to issuing corporations that have a total commercial paper program size in excess of five hundred million dollars (\$500,000,000.00).

In determining the approved securities, the Secretary-Treasurer may rely on any information or designation maintained and approved by the Treasurer of the State of Missouri.

All trades, where applicable, will be executed by delivery vs. payment (DVP) to ensure that the securities are deposited in eligible financial institutions prior to the release of funds. All securities shall be perfected in the name or for the account of the District and shall be held by a third-party custodian and evidenced by safekeeping receipts.

"Approved Depository Banks" means any bank, trust company, or savings and loan, selected by the Secretary-Treasurer and approved by the Board.

Repurchase transactions will be executed only with Primary Dealers or financial institutions located in the State of Missouri that qualify under Securities & Exchange Commission Rule 15C3-1 (Uniform Net Capital Rule) with whom the District has executed a Master Repurchase Agreement. In addition, local financial institutions, with whom there is a Master Repurchase Agreement, may be used for late-in-the-day transactions or regular cash account sweeps. In all cases, repurchase agreements shall be collateralized as provided in the section "Collateralization" of this Policy.

IX. INVESTMENT RESTRICTIONS

To provide for the safety and liquidity of the District's funds, the investment portfolio will be subject to the following restrictions:

- a. Borrowing for investment purposes ("Leverage") is prohibited.
- b. Instruments known as Structured Notes (e.g. inverse floaters, leverage floaters, and equity-linked securities) are not permitted. Investment in any instrument, which is commonly considered a "derivative" instrument (including options, futures, swaps, caps, floors and collars), is prohibited
- c. Contracting to sell securities not yet acquired in order to purchase other securities for purposes of speculating on developments or trends in the market is prohibited.
- d. No more than 5% of the total market value of the portfolio may be invested in banker's acceptances issued by any one commercial bank and no more than 5% of the total market value of the portfolio may be invested in commercial paper of any one issuer.

X. COLLATERALIZATION

Collateralization will be required on (1) repurchase agreements, (2) time certificates of deposit and (3) deposits with banking institutions. All securities pledged as collateral shall

be held in a segregated account on behalf of the District by an independent third party with whom the District has a current custodial agreement and that has been designated by the Secretary-Treasurer and the Board as eligible to serve in such capacity. Clearly marked evidence of ownership (safekeeping receipt) must be supplied to the District and retained. The right of collateral substitution may be granted.

The **market** value of any collateral shall be measured on the 15th day and last day of each month, or more frequently if determined by the Secretary-Treasurer. In the event the market value of the collateral no longer satisfies the collateralization level required, then the repurchase agreement provider or depository, as appropriate, shall provide additional collateral within two business days to satisfy the required level. The maturity of the pledged collateral shall not exceed the maximum specified in the Section "Maximum Maturity" of this Policy.

Repurchase Agreements. In order to anticipate potential market changes and provide a level of security for all funds, the collateralization level shall be 103% of the amount of the repurchase agreement and shall be based on the **market** value of principal and accrued interest of the pledged collateral. Acceptable collateral for repurchase agreements shall consist of U.S. Treasury obligations or obligations of U.S. government agencies or instrumentalities that are eligible to be delivered via the Federal Reserve's Fedwire book entry system. Securities will be delivered to the District's designated Custodial Agent. Funds and securities will be transferred on a delivery vs. payment basis.

Time Certificates of Deposit and Deposits with Banking Institutions. In order to anticipate potential market changes and provide a level of security for all funds, the collateralization level shall be 103% of the amount of the time deposits and demand deposits with any depository (less the amount, if any, which is subject to federal deposit insurance) and shall be based on the **market** value of principal and accrued interest of the pledged collateral. Acceptable collateral for time certificates of deposit and deposits with banking institutions shall consist of U.S. Treasury obligations or other interest-bearing securities guaranteed as to principal and interest by the U.S. or an agency or instrumentality of the U.S. (and approved by the state Secretary-Treasurer).

All securities, which serve as collateral against the deposits of a banking institution, must be safekept at a non-affiliated custodial facility. Banking institutions pledging collateral against deposits must, in conjunction with the custodial agent, furnish the necessary custodial receipts within five business days from the settlement date.

The District shall have a *depository contract and pledge agreement* with each bank that will comply with the Financial Institutions, Reform, Recovery and Enforcement Act of 1989 (FIRREA). This will ensure that the District's security interest in collateral pledged to secure deposits is enforceable against the receiver of a failed financial institution.

XI. MAXIMUM MATURITIES

To the extent possible, the District shall attempt to match its investments with its anticipated cash flow requirements. The District will not directly invest in securities or make a time deposit with a stated maturity of more than five years from the date of purchase. The average maturity for collateral provided to the District for deposits or in connection with a repurchase agreement shall not exceed five years without the written approval of the Secretary-Treasurer.

Because of inherent difficulties in accurately forecasting cash flow requirements, a portion of the portfolio should be continuously invested in readily available funds such as in

bank deposits or overnight repurchase agreements to ensure that appropriate liquidity is maintained to meet ongoing obligations.

XII. DIVERSIFICATION

The investments shall be diversified to minimize the risk of loss resulting from over concentration of assets in specific maturity, specific issuer, or specific class of securities. Diversification strategies shall be established and periodically reviewed. At a minimum, diversification standards by security type and issuer shall be:

- a. U.S. treasuries and securities having principal and/or interest guaranteed by the U.S. Government100%
- b. Collateralized time and demand deposits.....100%
- c. U.S. Government agencies, and government sponsored enterprisesno more than 60%
- d. Collateralized repurchase agreementsno more than 50%
- e. U.S. Government agency callable securitiesno more than 30%
- f. Commercial Paper.....no more than 30%
- g. Bankers' Acceptances.....no more than 30%

XIII. AUTHORIZED SECURITIES DEALERS AND DEPOSITORY BANKS

Pursuant to the Plan, the Secretary-Treasurer shall maintain a list of Authorized Depository Banks and Securities Dealers. The Secretary-Treasurer shall select those financial institutions that, in his or her opinion, will be most commensurate with the safety of District funds. In order to assist the Board, the Secretary-Treasurer shall employ a formal competitive procurement process for selecting financial institutions for the deposit of District funds, as well as for selecting broker/dealers for purchase of securities and for other banking-related services.

Securities Dealers. For brokers and dealers of government securities the Secretary-Treasurer shall select only primary government dealers that report daily to the New York Federal Reserve Bank or meet the Uniform Net Capital Rule (Rule 15C3-1) of the Securities and Exchange Commission, any Authorized Depository Bank, or any securities dealer with offices in the District or otherwise approved by the Secretary-Treasurer. Any firm seeking to qualify as a securities dealer shall supply the Secretary-Treasurer, on behalf of the Board, the information requested by Secretary-Treasurer as a part of the review process described above. The requested information shall be determined by the Secretary-Treasurer.

XIV. PERFORMANCE BENCHMARK

The investment portfolio as maintained is invested to provide funds as needed and specified by the direction of the various departments of the District. Given this strategy, the basis used to determine whether market yields are being achieved shall be the ninety day U.S. Treasury Bill.

XV. REPORTING

The Secretary-Treasurer shall provide the Board monthly investment reports which provide a clear and accurate picture of the current status of the investment portfolio. The Secretary-Treasurer's report should include comments on the fixed income markets and

economic conditions and such other matters as Secretary-Treasurer's believes necessary. The monthly report shall also include a prospective overview to the Secretary-Treasurer's investment strategy for the succeeding monthly period. The monthly report shall contain schedules that provide the following:

- a. A listing of individual securities held at the end of the reporting period;
- b. For each individual security listed, the report shall include: coupon, yield, par value, amortized book value and market value;
- c. Percentage of the portfolio represented by each investment category;
- d. For any time certificates of deposit, deposits with banking institutions or any repurchase agreements, a listing of the collateral pledged to such investments; and
- e. Additional information related to the portfolio as the Secretary-Treasurer deems necessary.

XVI. CONFLICTS WITH CONSTITUTION OF MISSOURI

The Plan provides that the District may invest "funds not immediately needed for the purpose to which said funds are applicable, in the same manner as the state treasurer may invest funds of the State of Missouri pursuant to Section 15, Article IV of the Constitution of Missouri, as amended from time to time." This Policy is intended to conform to the provisions of the Constitution of Missouri and to provide the District the same investment alternatives and limitations as the state treasurer under the Constitution of Missouri. In interpreting the provision of this Policy, the provision of Section 15, Article IV of the Constitution of Missouri, as amended from time to time, shall govern and provisions of this Policy shall be interpreted in a manner consistent therewith.

XVII. ADOPTION OF POLICY

Exemption. Any investment currently held that does not meet the guidelines of this Policy shall be exempt from the requirements of this Policy. At maturity or liquidation, such monies shall be reinvested only as provided by this Policy.

Adoption. This Policy shall be adopted by resolution of the District. The Policy shall be reviewed annually by the Board and recommended changes will be presented to the Board for consideration.

The Board of Trustees for the Metropolitan St. Louis Sewer District hereby adopts this Policy pertaining to investment of District funds this 8th day of February 2001.