AMEND POLICY NUMBER 00-0426-PO2
CHICAGO PUBLIC SCHOOLS INVESTMENT POLICY

THE CHIEF EXECUTIVE OFFICER RECOMMENDS:

That the Chicago Board of Education adopt the amended Chicago Public Schools Investment Policy.

POLICY TEXT:

CHICAGO PUBLIC SCHOOLS INVESTMENT POLICY – INTRODUCTION

The intent of the Investment Policy of the Board of Education of the City of Chicago ("Investment Policy") is to define the parameters within which funds are to be managed. This Investment Policy is approved by the Board of Education of the City of Chicago (hereinafter referred to as the "Board," the "Chicago Public Schools," or the "CPS"). The Board is responsible for maintaining schools in District 299. "CPS" shall refer to the administrative staff responsible for the day to day operations of the Board. CPS recognizes its responsibilities with respect to the use and custody of public funds. It is the policy of CPS to manage public funds in a manner which will meet cash flow needs, insure security, and provide the highest investment return while complying with all state and local requirements governing the investments of public funds. All investment transactions subsequent to the adoption of this policy adoption shall be in compliance with the provisions hereof.

The comprehensive policy will define the following:

I. Purpose
II. Investment Objectives and Standards
III. Scope of Policy
IV. Ethics and Conflicts of Interest
V. Authority
VI. Authorized Financial Dealers and Institutions
VII. Authorized and Suitable Investments
VIII. Description of Investment Portfolio Structure
IX. Safekeeping and Collateral
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I. Purpose

This document specifies policies, guidelines and criteria governing investments of all public funds held by the Chicago Public Schools in the course of its operations and mission as provided for in the Public Funds Investment Act 30, ILCD 235/1 et seq. (the "Investment Act") and other applicable law.

II. Investment Objectives and Standards

It is the policy of the Chicago Public Schools to invest public funds in a manner which is consistent with all state and local laws governing the investment of public funds and which will meet the following objectives:

- **Prudence**
  The standard of prudence to be used shall be the "prudent person" standard and shall be applied in the context of managing an overall portfolio. Persons authorized to trade on behalf of CPS acting in accordance with written procedures, this Investment Policy, and exercising due diligence shall be relieved of personal responsibility for an individual security's credit risk or market price changes.

  Investments shall be made with 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.

- **Safety of Principal**
  Investments of the Chicago Public Schools shall be undertaken in a manner that provides for the preservation of principal in the overall portfolio.

- **Diversification**
  The Chicago Public Schools shall diversify its investments to avoid incurring unreasonable risks associated with specific securities or financial institutions.

- **Liquidity**
  The investment portfolio of the Chicago Public Schools shall be sufficiently liquid to meet all reasonably anticipated operating and cash flow requirements.

- **Rate of Return**
  The investment portfolio of the Chicago Public Schools shall be constructed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account investment risk constraints and liquidity needs. While return on investment is of less importance than the safety and liquidity objectives described above, the investment program may seek to augment returns consistent with risk limitations identified herein and with prudent investment principles.

- **Public Trust**
  All participants in the investment process shall seek to act responsibly as custodians of the public trust and shall avoid any transactions that might impair public confidence in the Chicago Public Schools.

- **Portfolio Management**
  The Board recognizes and authorizes the Treasurer to develop procedures regarding trading practices that it deems appropriate to meet the investment objectives of this Investment Policy. Those procedures shall be presented to and reviewed by the CPS Investment Committee as appropriate, but at least annually.

III. Scope

This Investment Policy generally applies to all funds of the Chicago Public Schools. Certain funds may be subject to additional restrictions. School internal accounts are generally subject to this policy, except for the selection of financial institutions, which institutions do not need to be included in the City of Chicago's approved depository listing.

IV. Ethics and Conflict of Interest

In addition to all obligations and requirements of the Board's Ethics Policy, all persons authorized to trade on behalf of CPS 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. The Treasurer shall implement an annual attestation to be completed by all personnel authorized to trade disclosing all personal brokerage relationships. The Treasurer shall collect and review such attestations and file them with the internal audit function.

Under no circumstances shall a participant in the investment process receive any type of financial gain, either directly or indirectly, from the investment of Chicago Public Schools funds. Any real or potential conflict of interest must be reported to the internal audit function and General Counsel.

V. Authority

The Illinois School Code, 105 ILCS 5/34-28

Public Funds Investment Act 30 ILCS 235/1 (et seq.)

The Chicago Public Schools may direct its investments in accordance with the Investment Act.

Pursuant to Chicago Public Schools Rule 5-28, the investment authority rests with the Treasurer of the Chicago Public Schools as delegated by the Chief Fiscal Officer. (See Appendix A for defined responsibilities of the Treasurer.)

No person may engage in an investment transaction except as provided under the terms of this Investment Policy and the procedures established by the Bureau of Treasury. The CPS Treasurer will be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate employees. The Treasurer may also delegate trading activity to Treasury staff.

VI. Authorized Financial Dealers and Institutions

Depositories

Deposits made by the Chicago Public Schools with financial institutions consist of checking accounts, savings accounts, NOW accounts and certificates of deposit. Deposits of Chicago Public Schools funds, with the exception of school internal accounts as designated by the Board, must be made with financial institutions on the City of Chicago's approved depository listing. In compliance with the Investment Act, reasonable efforts shall be made to deposit money in minority owned banks.

The Chicago Public Schools Treasurer shall maintain a list of approved security broker/dealers selected pursuant to standards established by the Treasurer and approved by the Investment Committee. In compliance with the Investment Act, reasonable efforts shall be made to do business with minority owned brokers/dealers. The Chicago Public Schools' Bureau of Treasury shall establish procedures for monitoring and shall annually review the approved broker/dealer list to ensure that all relationship risks including, but not limited to, counterparty, transaction, delivery and execution, are determined to be negligible with each and every approved broker/dealer.

VII. Authorized and Suitable Investments

Investments made must comply with the Investment Act and other applicable law. Such investments include:

1. Bond notes, certificates of indebtedness, treasury bills or other securities guaranteed by the full faith and credit of the United States as to principal and interest.

2. U.S. agency and instrumentality obligations which are limited to the following issuers:
    - Federal Home Loan Bank (FHLB)
    - Federal Home Loan Mortgage Corporation (FHLMC)
    - Federal Farm Credit Bank (FFCB)
    - Government National Mortgage Association (GNMA)
    - Federal Agricultural Mortgage Corporation (FarmerMac)
    - Tennessee Valley Authority (TVA)
    - Federal National Mortgage Association (FNMA)
    - 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, interest-bearing time deposits or any other investments constituting direct obligations of any bank as defined by the Illinois Banking Act, including bankers' acceptances and bank notes. 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 ratings 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.

4. Other Depository investments such as Interest-bearing certificates of deposit, interest-bearing time deposits or any other investments constituting direct obligations of any bank as defined by the Illinois Banking Act, including bankers' acceptances and bank notes may be purchased at approved City of Chicago Depositories. Approved depositories who do not carry the required rating gradation from S&P or Moody's, as referenced above, must provide approved collateral as referenced in Section IX of this policy

~~4.~~5. Short-term obligations of corporations organized in the United States, including, but not limited to Student Loan Marketing Association (SLMA) bonds and discount notes, commercial paper, corporate bonds, and master notes, if: 1) assets of the corporation exceed $500,000,000; and 2) such obligations mature not later than 180 days from the time of purchase; and 3) such purchases do not exceed 10% of the corporation's outstanding debt; and 4) such obligations are rated by at least 2 rating agencies, one of which must be S&P or Moody's, with rating, maturity, and asset allocation limits at the time of purchase as follows:

Aggregate Allocation: $\leq$ 30% of total funds

Short-term ratings in the highest classification without regard to gradation: $\leq$ 30% of total funds and maturities of $\leq$ 180 days

Short-term ratings in one of the highest 2 classifications and long-term ratings in one of the highest 3 classifications without regard to gradation: $\leq$ 15.0% of total funds and maturities of $\leq$ 90 days

~~5.~~6. 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 paragraphs (1) and (2) of this section and to agreements to repurchase such obligations and that such fund has a short-term rating of "AAAm" by S&P.

~~6.~~7. Interest bearing bonds or notes of any county, township, city, village, incorporated town, municipal corporation, or school district. The bonds shall be registered in the name of the municipality or held under a custodial agreement at a bank. The bonds shall have a long-term rating in one of the highest 2 classifications without regard to gradation at the time of purchase by a rating service of nationally recognized expertise in rating bonds of states and their political subdivision.

~~7. Short-term discount obligations of the Federal National Mortgage Association.~~

8. Public Treasurer's Investment Pool created under Section 17 of the State Treasurer Act with a short-term rating of "AAAm" by S&P.

9. A fund managed, operated, and administered by a bank, subsidiary of a bank, or subsidiary of a bank holding company, provided that the portfolio of any such fund is limited to dollar-denominated securities described in paragraphs (1), (2), (3), ~~and~~ (4), and (6) of this section and to agreements to repurchase such obligations and provided that the Board has an undivided interest in the assets of the fund. The securities purchased by the Fund are subject to the quality, diversification, and other requirements of Rule 2A-7 under the 1940 Act and other rules of the SEC.

10. Repurchase agreements pursuant to the Investment Act. The securities, unless registered or inscribed in the name of the Board, 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 Board 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 Board is authorized to acquire under law, may be acquired pursuant to agreements entered into between the Board (or a trustee or agent on behalf of the Board) and suppliers of such securities under which agreements suppliers agree to sell to the Board (or any such trustee or agent) 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.

VIII. Description of Investment Portfolio Structure

The Chicago Public Schools recognizes the need for a prudent, professional, and practical approach to the investment of its funds.

The Treasurer is responsible for ensuring that cash flow forecasts are created, updated and reviewed as necessary to ensure liquidity needs are identified and met. The investment strategy must provide for portfolio liquidity and safety of principal above all other considerations.

The Operating Fund shall maintain a portfolio structure consisting of a two-tiered investment philosophy with the following tier structure: Liquidity Cash Management and Enhanced Cash Management.

The Chicago Public Schools shall maintain liquid balances that reflect the cash flow needs. If the Chicago Public Schools' funding structure or revenue and disbursement cycles change significantly, the Treasurer shall make appropriate recommendations to the Investment Committee for modifications of these fund groups and characteristics therein.

NAME: LIQUIDITY CASH MANAGMENT (LCM)

Objective: To provide for all operating needs of the CPS on a day to day basis.

Guidelines: The purchase of securities outlined in the authorized listing. The average maturity of the portfolio should not exceed 6 months.

Asset Allocation Range: The market value of this pool should reflect cash flow requirements at the discretion of the Treasurer, with a minimum of 110% of cash flow needs

Evaluation Benchmark: Merrill Lynch 3 Month Treasury Bill Index or similar index

NAME: ENHANCED CASH MANAGEMNT (ECM)

Objective: To provide for the longer term investment of funds using established investment approaches as well as money management firms under contract with the Chicago Public Schools.

Guidelines: The purchase of securities outlined in the authorized listing. Average portfolio adjusted duration should not exceed the duration of the Merrill Lynch Government 1-5 Index or similar index ± 15%. Average portfolio maturity will not exceed 5 years. Maximum maturity of any single issue will not exceed 10 years.

Asset Allocation Range: The market value of this pool should reflect the excess of cash flow requirements and short-term liquidity desired as determined by the Treasurer. This pool represents assets that are not expected to be needed for 24 months or longer.

Evaluation
Benchmark: Merrill Lynch Government 1-5 Index or similar index

On a quarterly basis, the performance of each investment tier will be compared to the defined relevant benchmark index, and, secondarily, to an appropriate universe of investment management firms. Over time periods of 3 to 5 years, it is expected that any external investment managers will produce results that exceed the return of the evaluation benchmark index on a net of fees basis.

IX. Safekeeping and Collateral

All Chicago Public Schools investment securities shall be held by a third party custodian in accordance with municipal ordinances to the extent required by state statute. The Chicago Public Schools Treasurer shall periodically review the approved depositories to evaluate counterparty risk. (See Appendix A for defined responsibilities of the custodian.)

The Chicago Public Schools shall require collateral of not less than 110% of the original acquisition price, including principal and accrued interest, on depository account balances, certificates of deposit, bankers' acceptances, and bank notes, unless either: 1) the bank has assets exceeding $500,000,000; or 2) the applicable instrument is insured at the time of purchase by an entity with long-term ratings in one of the highest 2 classifications without regard to gradation, in which case collateralization is not required. Repurchase agreement collateral shall be not less than 102%.

Collateral shall be held in the Chicago Public Schools' name by an independent third party custodian. Collateral is limited to investments authorized in Section VII. The Chicago Public Schools Bureau of Treasury must approve of any substitution of collateral. The Chicago Public Schools Bureau of Treasury shall monitor collateral for funds under control of the Treasurer on a monthly basis requiring additional collateral when the ratio falls below the designated level, and release collateral when the ratio exceeds the required level. Each individual school shall be for monitoring its internal accounts to ensure collateral compliance.

Notwithstanding the foregoing provisions of this Section IX, the Chief Fiscal Officer of the Board may direct any trustee under an indenture securing notes or bonds of the Board to enter into a Tri-Party Custodian Undertaking with a bank or trust company for the purpose of holding and valuing (as such trustee's agent) securities that are the subject of a repurchase agreement entered into by the trustee pursuant to such indenture.

X. 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:

Market Risk - the risk that the value of a security will rise or decline as a result of changes in market conditions.

Control Technique - the Bureau of Treasury shall provide for mark to market valuations on a monthly basis.

Credit Risk - the risk that an issuer will default in the payment of interest and/or principal on a security.

Control Technique - the Bureau of Treasury will limit investments to the safest types of securities, pre-qualify the financial institutions, broker/dealers, intermediaries and advisers with which the Chicago Public Schools will do business, and diversify the investment portfolio so that potential losses on individual securities will be minimized. The Bureau of Treasury shall provide ongoing evaluation and monitoring of creditworthiness of all counterparties.

Liquidity Risk - the risk that an asset cannot be converted quickly and easily into cash.

Control Technique - the Bureau of Treasury 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 Chicago Public Schools is also required to participate in the risk management process and adhere to the Objectives and Standards outlined in Section II.

XI. Accounting

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

XII. Arbitrage

The Chicago Public Schools may at times have responsibility for arbitrage rebate calculations under Federal government regulations in connection with the issuance of debt by the Chicago Public Schools, or debt issued by others on behalf of the Chicago Public Schools. These regulations can limit or cause the Chicago Public Schools to rebate interest earnings to the federal government. These calculations and procedures are very complex and if the Chicago Public Schools has possible responsibility under these rules, the Chief Fiscal Officer shall procure professional legal and accounting counsel with respect to the arbitrage calculations.

XIII. Internal Controls

The Treasurer shall establish a system of internal controls, which shall be documented and reviewed by the CPS Investment Committee. The controls shall be designed to prevent losses of Chicago Public Schools funds arising from fraud, employee error, misrepresentation by third parties, or imprudent actions by employees.

XIV. Investment Committee

The Chief Fiscal Officer shall appoint an Investment Committee that will meet at least quarterly with the Treasurer. The Treasurer may call more frequent meeting as deemed necessary. (See Appendix A for defined responsibilities of the Investment Committee.)

XV. Investment Performance and Reporting

The Treasurer is responsible for preparing monthly investment reports and providing them to the CPS Investment Committee monthly. The Treasurer shall report on the following types of information:

1. Mark-to-market adjustment on the portfolio by security type
2. Commentary on general direction of the market
3. Market exposures and position balances by investment balances
4. Credit exposures arising from downgrades, repurchase agreements, etc.
5. Current cash balances, projected future cash flows, funding requirements and any borrowing required.
6. Comparison of actual return to forecast and to appropriate evaluation benchmark returns.
7. Changes in the perceived or actual risk of any component of the Chicago Public Schools' portfolio.
8. Returns of the portfolio according to the 2 tiers of investment criteria
9. Results and returns on investments of each of the outside money managers.
10. Discussion of any policy violations.
11. Other reports as requested by the CPS Investment Committee

In addition, the CPS Investment Committee shall generally discuss the portfolio and provide input into such matters as asset allocation and money management.

~~III.~~ XVI. Professional Money Management Advisory Services

The Chicago Public Schools reserves the right to contract out investment advisory services to professional money managers using the following criteria for selection:

- experience as fixed income manager
- public sector expertise
- effective and appropriate portfolio management strategies
- cost effective
- staff resources

Contracts may be on a non-discretionary or discretionary basis, and all investment managers shall be subject to this Investment Policy. (See Appendix A for defined responsibilities of professional money managers.)

XVII. Prohibited Transactions

The following transactions are not in compliance with current applicable law and are prohibited:

- When Issued Trading - trading of security prior to its issuance
- Reverse Repurchase Agreements - the loaning of Chicago Public Schools securities for cash proceeds
- Securities Lending - the loaning of Chicago Public Schools securities for other securities
- Short Selling - the sale of a security the Chicago Public Schools does not own
- Any purchase of securities not authorized in Section VII. The Board must approve of new security types.

- Collateralized Mortgage Obligations Investments whose returns are linked to or derived from the performance of some underlying asset or index such as bonds, currencies or commodities. Examples of this are range notes, inverse floaters or any other kind of embedded option IOs, POs, CMO Residuals, Z-Tranche CMOs, and other derivatives that are speculative in nature are prohibited. The use of instruments that would cause the portfolios to be in any way leveraged is also strictly prohibited. Treasury or agency securities that have a call option are not included in this prohibition.

~~IV.~~ XVIII. Investment Policy Adoption

The Chicago Public Schools' investment policy shall be adopted by resolution of the Board. The policy shall be reviewed annually by the Treasurer and the CPS Investment Committee, and any modifications thereto shall be approved by resolution of the Board.

XIX. Correction of Noncompliance

As a result of changes in the market, the Investment Act or other applicable law, current holdings could fail to meet the guidelines of this policy. Whenever that occurs, the Treasurer will immediately notify the Chief Fiscal Officer, and appropriate action will be taken.

XX. Appendix A

Definition of Responsibilities

Responsibilities of the Treasurer include, but are not limited to, the following:

1. Produce cash flow forecasts to identify CPS' cash flow needs

2. Structure a portfolio which meets CPS' cash flow needs and ensures safety of principal and a reasonable market rate of return and protects against fraud, employee error, misrepresentation by third parties, or imprudent actions by employees

3. Develop a system of internal controls to assure compliance with this Investment Policy and investment objectives

4. Establish procedures for monitoring and annually reviewing CPS' broker-dealers

5. Provide monthly investment reports as specified in this Investment Policy to the Investment Committee at least quarterly

6. Develop policies regarding trading practices which meet the objectives of this Investment Policy

Responsibilities of the Investment Committee include, but are not limited to, the following:

- Review the reports provided by the Treasurer to monitor compliance with the Investment Policy

- Review and discuss investment strategy and trading practice

- Review relationships with financial institutions, including broker/dealers, to ensure that financial institutions are being selected and reviewed in accordance with Treasury procedures

- Monitor use of all CPS funds, including bond funds, to ensure appropriateness and compliance with CPS Investment Policy and objectives

- Review policies regarding trading practices

- Review the system of internal controls established by the Treasurer

Responsibilities of the Professional Money Managers include, but are not limited to, the following:

- Manage the portion of the Chicago Public Schools' investment portfolio under their control in accordance with the policy objectives and guidelines as established.

- Comply with any applicable legal or regulatory stipulations.

- Exercise full investment discretion as to buy, hold and sell decisions for all assets under management within the investment guidelines established herein.

- Promptly inform the Treasurer of significant matters pertaining to the investment of the assets.

- On a quarterly basis, provide the following:
  - A written review of investment performance and portfolio structure.
  - A synopsis of key investment decisions, rationale and expected future implications.
  - An organizational update, including a report on any and all changes in organizational structure, staffing, investment processes and strategies and asset base.

- Meet with the Treasurer and/or Investment Committee as requested.

- Reconcile security market values and cash flows with the Custodian on a monthly basis.

Responsibilities of the Custodian(s) include, but are not limited to, the following:

- Act in accordance with relevant custody agreements.

- Report all financial transactions to the Treasurer and prepare periodic summaries of transactions, asset valuations and other related information as requested.

- Reconcile security market values and cash flows with the Investment Manager on a monthly basis.

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