Sample Investment Policy for Credit Unions

ANY FEDERAL CREDIT UNION

ANYTOWN, ANYSTATE

Your Date 20XX

<table>
<thead>
<tr>
<th>BOARD POLICY:</th>
<th>XX-2</th>
</tr>
</thead>
<tbody>
<tr>
<td>SUBJECT:</td>
<td>Board of Directors’ Policy on Investments</td>
</tr>
<tr>
<td>PURPOSE:</td>
<td>-Establish investment policy for the financial assets of the credit union that have not been loaned out.</td>
</tr>
</tbody>
</table>

A. GENERAL

The board of directors of the ANY Federal Credit Union is charged with the responsibility to invest prudently and properly all funds that have not been loaned out to the members of the credit union. Because these funds may be called upon, it is essential that absolute maturity horizons are identifiable for the purpose of liquidity. In addition the board will ensure that investment of funds is accomplished in a safe and secure manner, particularly with respect to limiting the exposure of the credit union to unnecessary risk. The following investment policy addresses the methods, procedures, and practices that must be exercised to ensure effective and sound fiscal management.

SCOPE

This policy applies to investment activities of the ANY Federal Credit Union (hereinafter referred to as the “credit union”) with regard to investing the financial assets of all funds excluding loans.

INVESTMENT AUTHORITY

The ultimate responsibility and authority for investment transactions involving the credit union reside with the CEO, who is designated by the credit union’s board of directors to make investment decisions. The CEO, or designee, may consult with outside investment advisers and broker-dealers to assist in the investment management process. At all times, the CEO shall retain discretionary control over the purchase and sale of investments.

PRUDENCE

The standard of prudence to be used for managing the credit union’s assets is the “prudent investor” rule, which states, “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.” The credit union shall not assume default risk in an attempt to enhance return. All investments will be made in accordance with the Federal Credit Union Act, with state laws and within regulations as directed by the National Credit Union Administration (NCUA).
**RISK MANAGEMENT**

In establishing and maintaining an investment securities portfolio, the credit union may assume certain risks, including interest-rate risk, credit risk, liquidity risk, and operational risk. The credit union has developed a risk management program for effectively controlling each of these exposures.

**LIQUIDITY RISK**

Liquidity risk for an investment portfolio refers to the risk that the credit union will be unable to sell a security at or near its fair value because of lack of market depth. The credit union will control for this risk by adhering to its portfolio diversification and investment characteristic requirements.

Liquidity risk for the credit union also represents the risk that insufficient funds will be available to meet immediate cash demands. At least annually, management will assess the potential liquidity needs of the credit union for the coming year. This assessment will include those needs caused by potential increases in loan demand and changes in share account balances. Management will use historical data in preparing this analysis. Furthermore, the assessment will include a plan for meeting these potential needs. It is anticipated the plan will consider liquidity to be provided by scheduled maturities of investments, sales of investments classified as available-for-sale, borrowing, and potential changes in pricing strategies. The assessment will be formally reviewed and accepted by the board of directors.

**INTEREST-RATE RISK**

For the purposes of this policy, interest-rate risk (IRR) is defined as the risk that the market value of an individual security and/or the investment portfolio may decline due to an adverse movement in interest rates. Management and the board of directors understand that IRR is an important risk factor in investing activities and have established policies and practices to rigorously identify, measure, monitor, and control the exposure.

- Prior to purchase, certain securities will be subject to preacquisition analysis for purposes of identifying risk elements and ensuring compliance with policy guidelines. However, should the incremental effect of any investment position have a significant effect on the IRR profile of the entire portfolio, the credit union will also measure the impact on the aggregate price sensitivity of the portfolio prior to making the purchase. Refer to “Prepurchase Risk Analysis” for a description of required analysis and documentation.

- On an ongoing basis, the credit union will measure the potential price sensitivity of individual securities and the entire investment portfolio under different rate environments. The valuation methodology for assessing IRR will be based on immediate and sustained parallel shifts in the yield curve (plus and minus 100 and 300 basis points). This analysis will take into account the fact that some instruments possess cash flows that vary as yields change. Cash-flow projections for mortgage securities and CMOs under the modeled rate environments will be based on Bloomberg median prepayments or, when Bloomberg data is not available, the projections of major dealers.

- To control the level of IRR in any single instrument, the following limits are established:
  1. An investment in an authorized security (other than a mortgage security) is limited to a maximum final maturity of five years.
2. Investments in mortgage securities and CMOs are subject to the following limits:
   a. Fixed-rate mortgage investments must have a weighted average life (WAL) at the time of purchase of five years or less.
   b. At the time of purchase, the estimated percentage price decline of a mortgage security under a 300-basis-point adverse shift in interest rates may not exceed 15 percent.
3. The maximum maturity or WAL parameters shall not apply to investments in any adjustable, variable, or variable-rate security, including floating-rate CMOs and adjustable-rate mortgage-backed securities, or any SBA security as long as the instrument reprices or resets no less often than annually and the current coupon on the instrument is less than at least 300 basis points below the contractual rate cap.
4. Unless approval by the board of directors is obtained prior to purchase, the credit union may not acquire a security if the estimated price sensitivity of the instrument causes the credit union to exceed its IRR limit for the total investment portfolio.
   • To control the level of IRR in the total investment portfolio, the following limits are established:
   1. In any reporting period, the percentage price decline of the total portfolio under a 300 basis point adverse shift in interest rates may not exceed 9 percent.
   2. The projected decline of the market value of the portfolio under an adverse shift in rates of 300 basis points may not exceed 10 percent of the credit union’s net capital.

CREDIT RISK
Credit risk refers to the risk that an issuer will fail to perform on an obligation to the credit union. Prior to making an investment, the credit union will determine the issuer’s creditworthiness and ensure the obligation meets the highest quality standards. Obligations of the U.S. government or its agencies, enterprises, or corporations and obligations fully insured by NCUA or FDIC (including accrued interest) possess very low credit risk and are exempt from prepurchase credit analysis requirements.

The asset-liability committee shall maintain, and the board of directors shall approve, a list of approved financial institutions in whose obligations and uninsured deposits the credit union may invest. The chief financial officer or an appointed staff member annually will perform a written evaluation of the safety and soundness of each approved financial institution in which the credit union has an uninsured deposit. This evaluation will at a minimum analyze the historical three-year trend of (1) capital adequacy, (2) asset quality, (3) earnings performance, and (4) liquidity ratios for each institution being reviewed. Also, the issuer’s credit rating as determined by a nationally recognized statistical rating organization will be reviewed, if available.

The ALCO will review at least annually the financial statement of ANY Federal Credit Union’s corporate credit union, the quality and diversification of the investments of the corporate, and the investment policies of the corporate—including its investment analysis procedures—and find that such investments are made in an acceptable manner and in keeping with the safety and soundness of the credit union.
   • For corporate credit unions, the NEV ratio and operating level under Regulation 704 will also be evaluated.
OPERATIONAL RISK

The credit union faces operational risk when deficiencies in information systems or internal controls result in unexpected loss. Operational risk in the investment portfolio will be controlled with the following procedures:

**Safekeeping.** Investment securities purchased by the credit union will be delivered by book entry and settled on a delivery versus payment basis. The board will approve all safekeeping agents. U.S. Central Credit Union, Overland Park, Kansas, and ANY Federal Credit Union’s corporate credit union, Arvada, Colorado, are approved as third parties for the purposes of safekeeping of securities. The safekeeping agents as designated shall provide both a written confirmation of each transaction to the credit union and a monthly listing of all securities maintained in the account of the credit union. These statements will be reconciled with the credit union’s records.

**Securities valuation.** Prior to entering into a securities transaction, at least two quotes will be obtained. At least one quote will be from a broker-dealer, and the other may be from either another broker-dealer or from an industry-recognized information provider (for example, Bloomberg, a newspaper). The “ALLQ” screen, printed from Bloomberg, is also acceptable documentation of an indicative price. Only one quote is necessary if the issue is purchased while in syndicate and priced at par or for a new issue of a security purchased at original issue discount. If the credit union does not execute the transaction with the broker-dealer with the best quote, a justification should be provided. Acceptable reasons for this include compensation for services or initially presenting the trade idea, among others.

- The monthly computation of investment portfolio fair value will be based on securities prices obtained from sources independent of the credit union.
- At least annually, a supervisory committee of the credit union or an independent auditor will verify the reasonableness of investment market values. The review will be conducted in accordance with generally accepted auditing standards.

SOVEREIGN RISK

The credit union shall invest only in obligations of the U.S. government, government agencies, or domestic corporations, and financial institutions that are domiciled and regulated in the United States. The credit union shall invest only in dollar-denominated assets.

POLICY REVIEW

This investment policy shall be reviewed at least annually by the board of directors of the credit union, and any additions or deletions will be approved by the board of directors.

BOARD-APPROVED INVESTMENT ACTIVITY

The credit union may invest only in instruments that are specifically authorized in this section. All other investments are prohibited.

1. The CEO of the credit union is authorized to invest any portion or all of the credit union assets through ANY Federal Credit Union’s corporate credit union.

2. The following is a partial list of federal agency securities that are authorized investments for ANY Federal Credit Union:
<table>
<thead>
<tr>
<th>Name</th>
<th>Originally Approved by Board of Directors on</th>
<th>Deleted on</th>
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</thead>
<tbody>
<tr>
<td>FHLB</td>
<td>11/77</td>
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<tr>
<td>FHLMC</td>
<td>5/77</td>
<td></td>
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<tr>
<td>GNMA</td>
<td>2/88</td>
<td></td>
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<tr>
<td>SLMA</td>
<td>4/96</td>
<td></td>
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<tr>
<td>FNMA</td>
<td>12/97</td>
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Any other federal agency securities not prohibited by NCUA are also authorized investments under this section.

3. The following investments are permitted and authorized by the board of directors of the credit union.

A. Authorized Investments

<table>
<thead>
<tr>
<th>Permissible Sectors</th>
<th>% of Portfolio Concentration Limit</th>
</tr>
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<tbody>
<tr>
<td>1. ANY’s corporate credit union</td>
<td>100%</td>
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<tr>
<td>2. U.S. Treasury bills</td>
<td>100%</td>
</tr>
<tr>
<td>3. U.S. Treasury notes</td>
<td>100%</td>
</tr>
<tr>
<td>4. U.S. government agency securities</td>
<td>100%</td>
</tr>
<tr>
<td>5. Bank and S&amp;L certificates of deposit</td>
<td>100%</td>
</tr>
<tr>
<td>6. Federal funds sold</td>
<td>15%</td>
</tr>
<tr>
<td>7. Mortgage-backed securities (pools &amp; REMICs)</td>
<td>40%</td>
</tr>
<tr>
<td>8. Small Business Administration pools</td>
<td>20%</td>
</tr>
<tr>
<td>9. Money market funds</td>
<td>100%</td>
</tr>
<tr>
<td>10. Fixed-rate issues without embedded options (bullets)</td>
<td>100%</td>
</tr>
<tr>
<td>11. Overnight investments</td>
<td>100%</td>
</tr>
<tr>
<td>12. Issues with embedded call and/or put options (that is, callable agencies or certs, CMOs, MBS)</td>
<td>50%</td>
</tr>
<tr>
<td>13. MBS/CMOs (also subject to limit on issues with embedded call and/or put options)</td>
<td>40%</td>
</tr>
<tr>
<td>14. Floating-rate issues</td>
<td>25%</td>
</tr>
<tr>
<td>15. CUSO</td>
<td>100%</td>
</tr>
</tbody>
</table>

Concentration limits apply at time of purchase only. For issues that fall into more than a single category, limits for all applicable categories apply.
Floating-rate investments authorized under this policy must conform to the following guidelines:

1. The index associated with any floating-rate security must reference a single domestic interest rate with a maturity of one year or less. For purposes of this policy, U.S. dollar-denominated LIBOR is a domestic interest rate. The coupon formula must reset no less frequently than annually on a one-for-one basis with the reference index. Leveraged, range, dual-indexed, and inverse floating rate securities are not permissible investments.

2. The credit union is authorized to purchase floating-rate securities that possess embedded periodic and lifetime rate caps. However, the security’s coupon rate on the date of purchase must be a minimum of 300 basis points below the instrument’s lifetime cap.

B. Bank and S&L Certificates of Deposit

- Certificates of deposit of any institution whose deposits are insured by the FDIC may be purchased provided the face amount plus accrued interest does not exceed $100,000. Certificates of deposit in excess of $100,000 may be purchased from those institutions that have been approved by the board of directors after such institutions have been evaluated by the ALCO and deemed to be financially secure.

C. Credit Union Service Organization

- ANY FCU, with board approval, may invest in CUSOs up to the allowable NCUA limit.

FAS 115

Financial Accounting Standard 115 requires credit unions to categorize investments into one of three categories: hold to maturity, available for sale, and available for trade. The intent of ANY FCU is to have a portfolio composed of securities available for sale. Trading activities are expressly prohibited under terms of this policy.

REPORTING

At least monthly a report will be prepared listing all investments in the portfolio. For each investment the following information will be included:

- Amount
- Issuer
- Coupon
- Maturity date
- Call date (if applicable)
- Book value

For marketable securities, the report shall also include the change in market value over the past month, the current market value, and unrealized gains and losses.
For issues that have the following characteristics, additional requirements shall apply:

- embedded options (call options, put options, caps, and floors);
- maturities in excess of three years;
- inverse floaters, dual-index floaters, levered/delevered floaters.

Both marketable and nonmarketable issues with these characteristics shall be listed on a report that is provided to the board on a quarterly basis. The total book value for the marketable issues will be compared to the credit union’s capital (reserves, undivided earnings, unrealized gains/losses on AFS securities, and current period net income). If the value of these securities exceeds capital, a projected change in value of all securities given an immediate and sustained parallel shift of +/− 300 basis points shall be calculated. This amount will be compared to capital in both percentage and dollar terms.

**APPROVED ACTION LISTS**

The use of qualified and reputable broker-dealers to execute securities transactions is essential to the success of the investment portfolio. For this reason, only broker-dealers that have been approved by the board of directors may be used to execute securities transactions.

At least annually the ALCO will review the list of approved broker-dealers and will recommend to the board of directors any additions or deletions from the list. The ALCO shall retain documentation of the review information used to approve a bank or broker-dealer. In performing its review the ALCO shall take the following factors into account:

- the financial stability of each broker-dealer based on an analysis of financial statements (applicable only if the credit union safekeeps securities with or is involved in repurchase, reverse repurchase, or securities lending transactions);
- each broker-dealer’s reputation based on referrals from other credit unions and ANY Federal Credit Union’s experiences with each broker-dealer;
- any enforcement actions against a broker-dealer by federal or state regulators or the National Association of Securities Dealers;
- the experience, expertise, and background of any representative providing advice to the credit union.

All credit union investment activity shall be transacted through those dealers appearing on the attached “Approved Securities Dealers” list. Additionally, no director or credit union officer having investment authority shall maintain a personal investment account with any approved securities dealer.

The officials and senior management employees of the credit union must always conduct investment transactions in the best interest of the credit union. These individuals, as well as their immediate family members, may not receive anything of value in connection with investment transactions made by the credit union. This prohibition does not include compensation for employees.

The following is a list of broker-dealers that are approved to conduct investment transactions with the ANY Federal Credit Union:
<table>
<thead>
<tr>
<th>Name</th>
<th>Approved by Board of Directors on</th>
<th>Deleted on</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prudential-Bache</td>
<td>4/72</td>
<td></td>
</tr>
<tr>
<td>Corporate Network Brokerage Service (CNBS)</td>
<td>8/30/93</td>
<td></td>
</tr>
<tr>
<td>Goldman Sachs (TCU—Money Market Portfolio)</td>
<td>4/23/96</td>
<td></td>
</tr>
<tr>
<td>Multi Bank Securities (Certificates of Deposit)</td>
<td>4/23/96</td>
<td></td>
</tr>
<tr>
<td>Your Corporate FCU</td>
<td>11/16/99</td>
<td></td>
</tr>
<tr>
<td>Another Corporate FCU</td>
<td>11/16/99</td>
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**INVESTMENTS OUTSIDE POLICY OR REGULATION**

If an investment ceases to meet the provisions of this policy and/or regulations, the board of directors shall be so informed at its next regularly scheduled meeting. The board will also be presented with an analysis that discusses the merits of both holding and liquidating the investment. This analysis will consider:

- the amount of the investment relative to the credit union’s capital;
- remaining time to maturity;
- potential effect of liquidating the investment on capital;
- the possibility that the investment will again meet policy/regulatory requirements and the anticipated time frame for this to occur;
- the potential costs and/or benefits that could occur if the investment were liquidated or held;
- any steps that should be taken to monitor the investment on an ongoing basis.

If the investment is inconsistent with regulations, the NCUA regional director will be notified within five days of the board’s notification. A copy of the above analysis will be included with the notification. Board action regarding the investment will be noted in the minutes of the meeting, including an explanation of a decision not to sell a security that is inconsistent with the NCUA investment regulations.

**PREPURCHASE RISK ANALYSIS**

Certain instruments that the credit union is authorized to purchase will be subject to a risk assessment prior to acquisition. The purpose of the prepurchase risk analysis will be to fully demonstrate an understanding of the exposures and to show that prudence was exercised. The extent of prepurchase risk analysis and related documentation will be dependent upon the type of investment purchased. For all investments, a file shall be maintained that includes a description of the investment’s characteristics. The credit union shall maintain documentation for each security purchased as long as the
investment is held in portfolio and until the documentation is both audited and examined.

The credit union has experience with and understands the risks of investing in bullet, fixed-coupon investments, such as U.S. Treasury obligations, U.S. government agency securities, and debentures issued by U.S. government-sponsored enterprises. As these are standardized instruments, they not subject to prepurchase risk analysis. However, such instruments may not exceed this policy’s maturity limit.

When considering the purchase of complex investments, the credit union will perform analysis that captures all embedded risk, such as calls, caps, and floors. Investment types that must be analyzed prior to purchase include, but are not limited to, floating-rate securities, agency callable securities, mortgage pass-through securities, and CMOs. Prepurchase analysis will document the instrument’s various characteristics, including

- coupon and call structure;
- factors that influence the value of the embedded option(s);
- cash-flow variability;
- price sensitivity under different interest-rate scenarios;
- credit quality.

The documentation file may include one or more of the following, or additional analytical information as appropriate:

- prospectus;
- alternate yield analysis;
- call schedule;
- deal summary;
- Floater scenario pricing analytics;
- credit analysis;
- security description;
- yield-to-call/yield-to-maturity information;
- principal repayment table/window;
- option-adjusted spread (OAS) analysis;
- Bloomberg Graduated Risk Assessment Debenture Evaluation (GRADE) screen;
- WAL/price sensitivity stress testing.

B. ANY FCU CORPORATE CREDIT UNION AUTHORIZATION

ANY FCU will participate and maintain membership shares in the corporate credit union at the established rate set by the corporate credit union based on ANY FCU assets as of the end of each calendar year.

ANY FCU agrees to the terms of the open-end loan agreement of the corporate credit union to a maximum of $5 million, authorizing the chair or vice chair and the CEO or
CFO to execute the open-end loan agreement of the corporate credit union and to obtain advances on behalf of the ANY FCU.

Previous references: 11/16/99
Approved Board of Directors: 01/01/2000