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The policies in this chapter are designed for credit unions that intend to use DICO's Workbooook for Less Complex Institutions sufficient for most situations that may arise. The policies may not cover each and every situation and must be customized to meet each credit union's unique requirements.

The shaded text that appears in this chapter is customizable by your credit union. Numbers or values within customizable text that you can change will be further differentiated in bold typeface. When customizing this chapter, use your software's Find/Replace function to insert your credit union's name wherever "the credit union" (or a variation of this phrase) appears.

Text in boxes, such as this one, is background information, and can be deleted when you customize this file.

Note: Material from By-law No. 5 has been incorporated into this policy. Customizing it will provide your credit union with Central's policy recommendations. It is strongly suggested that credit union managers and boards consult the workbooks prepared by DICO for additional guidance that will help them comply with the By-Law.

The credit union believes that it is in keeping with the overall credit union philosophy to have appropriate and prudent policies, procedures and controls to manage the on- and off-balance sheet market risk of the institution.

Investment decisions must agree with the credit union's investment philosophy and with the *Credit Unions and Caisses Populaires Act, 1994*, sections 190 and 191.

Policy Objectives

To establish an overall framework of market risk management which ensures that the credit union faces limited exposure to all material risks.

To implement a policy that addresses:

- authorized types, limits and concentration of investments, other financial instruments and assets
- defined and prudent levels of decision-making authority
- identifying, measuring, providing for and recording market impairments.

Responsibility

The Treasurer-Manager is responsible for managing market risk in accordance with this policy and the annual business plan.

The credit union may engage outside consulting help in the management of market risk within the scope of this policy.

The Board of Directors is responsible for ensuring that any major variances to budget are identified and that appropriate corrective measures are implemented.

Policy Guidelines

The credit union will adhere to the following policy guidelines:

1. The credit union will adhere to all regulatory requirements, including those prescribed in:
   - the Act, sections 198 to 202
   - the Regulations, sections 66 to 72 of Regulation 76/95
   - DICO's Standards of Sound Business and Financial Practices.
2. The credit union will ensure that its Market Risk Management policy is consistent with other policies and meets the requirements of the Ministry of Finance's Guideline for Prudent Investment and Lending Policies and Procedures.
3. The credit union will adhere to its market risk management philosophy, and as much as possible to its annual business plan, with respect to market risk management.
4. The Treasurer-Manager will invest the credit union's excess liquidity in authorized financial assets to maximize yields while maintaining a high level of security.
5. The credit union will delegate decision-making authority, including approval authority for:
   - the purchase and redemption of investment exposures
   - large or complex transactions

   Where third-party brokerage services are used, limits and authorities must be communicated and acknowledged.
6. The credit union will establish investment portfolio limits and outline the required analysis for acquisition or lease of capital assets. It will also maintain adequate measuring, monitoring and reporting of its risk position and investment management. Summaries of measurements will be prepared for board review at each board meeting.
7. As a general rule, the credit union will not lease or acquire capital assets (i.e., fixed assets) unless prior approval from the Board of Directors is obtained. The board may designate approval authority to a board committee, provided that an appropriate business case analysis will be conducted and documented for each proposed investment. Business cases for capital asset expenditure must include:
   - reasons for acquisition
   - a comparison analysis of at least three sources
   - an outline of criteria used to determine the successful supplier, including but not limited to:
     - required features
     - quality measurements
     - reliability
     - service
     - maintenance cost

- acquisition cost
- alternatives considered to acquisition.

8. The credit union's assets will be managed in accordance with the requirements of this policy. If variances arise, then responsibility lies with the Treasurer-Manager to put in place measures to correct the variance and report the variance and corrective measures taken to the board.
9. At no time will an investment not allowed under this policy be purchased.
10. The board will ensure that staff and/or volunteers charged with carrying out this policy and managing investments and market risk will have the necessary training and experience. Sound procedures will exist for investment purchases/disposals that will ensure there are appropriate authorizations and registrations.
11. There will be segregation of duties for: transaction authorization, asset custody and transaction recording, or compensation controls consisting of periodic review and verification of transactions by independent persons (e.g., the Audit Committee).
12. The Audit Committee will ensure that appropriate evaluation methodologies are employed which are suitable to the instruments used.
13. Investments of the credit union will reflect, in order of priority:
    - safety of principal
    - liquidity
    - income
    - the needs of the credit union system
    - the social, economic and ethical well being of the community.
14. The credit union will maintain the required ratio of shares with Credit Union Central of Ontario.
15. The credit union will maintain the mandatory liquidity requirements as stipulated by the Act, sections 84 to 90 and the Regulations, sections 16 to 21.
16. The credit union will employ competent and qualified persons with appropriate experience to manage investments and market risk.

Authority Levels

Below is a sample list of assets that are permitted under the Market Risk Management policy. **Customize this information to suit the needs of your credit union. These are suggestions which your credit union may consider. See the structural risk management section of Financial Administration in this manual for further information.**

Assets which may be purchased as part of an investment portfolio are as follows:

- Central deposits
- Government of Canada treasury bills and bonds
- Provincial treasury bills, promissory notes and bonds

- Schedule I bank deposits and banker's acceptances issued by a bank with a DBRS rating of R-1 low or better
- Required number of shares to maintain membership in Central.

For the purchase of the assets listed above, the credit union will develop and maintain a list of authorized investment dealers.

Example: The following is a sample list of authorized investment dealers.

The credit union will invest with the following authorized dealers:

- **Credit Union Central of Ontario (Treasury department)**
- **RBC Dominion Securities**
- **ScotiaMcLeod.**

Investment limits are as follows:

Asset type	% of Portfolio	Maximum Term
Central deposits	no limit	5 years
Government of Canada treasury bills and bonds	no limit	5 years
Provincial government treasury bills and promissory notes with a DBRS rating of R-1 mid or better	20	1 year
Provincial government treasury bills and promissory notes with a DBRS rating of R-2 high or R-1 low	10	3 months
Provincial bonds with a DBRS rating of AA or better	20	5 years
Schedule I bank deposits and bankers' acceptances	20	1 year

Note: Include other asset types if required, such as Co-op Trust term certificates, corporate bonds, derivatives, and shares in other entities.

These limits will be in effect at the time of purchase, and are in relation to the size of the overall financial investment portfolio. After purchase, the limits may be temporarily surpassed.

To limit term risk, no more than 50 per cent of the portfolio may be invested for terms greater than one year. This limit is to apply at the time of purchase. Maturity of financial instruments purchased or held is defined as the remaining term to maturity.

The credit union will not hold any material investments in foreign currencies, in accordance with the Structural Risk Management policy.

To provide flexibility in investing and to allow the responsible officer to take advantage of market opportunities in the purchase of commercial paper, the limits may be surpassed so long as:

- the term is not extended beyond an additional 91 days

- the dollar limit is surpassed by no more than 25 per cent.

When such an extension is made, the officer responsible must note the particular reasons for the action on the "investment voucher" and report the action to the Senior Financial Officer.

This authority for extensions does not apply to unhedged investments denominated in a foreign currency.

The credit union will not purchase real estate for its own use, nor as an income-producing property (except as a mortgage to a member within the allowable mortgage limit).

The credit union will not invest in a subsidiary. The credit union may invest in an affiliate organization with express prior approval of the board of directors.

The aggregate of any single investment in one individual or their connected persons shall not exceed 1% of capital and deposits. The Act and Regulations place a limit of 1.25% of capital and deposits.

The purchase of derivative financial instruments is not allowable, except in conjunction with a league sponsored program such as Index-linked Terms, in accordance with the credit union's structural risk management policy.

Target Investment Levels

The credit union will attempt to maintain minimum liquidity levels of between 12 and 18 per cent (this should coincide with the liquidity risk management policy) of deposits and other debt liabilities. If liquidity is in danger of dropping below 12 per cent, corrective action will be undertaken (such as restrictions on loan growth and/or deposit campaigns), as stipulated in the Regulations, section 19 of Regulation 76/95. The credit union should plan for fluctuations in liquidity caused by layoffs, vacations, strikes, RSP season, bond season, etc.

Annual Business Plan

As part of its annual planning process for market risk management, the credit union will include estimates for investment dollar volumes of specified quality and yields by investment categories and by term. Projections of plans will be made on a monthly basis.

Reporting

A report on market risk management will be presented to the board of directors at each board meeting. This will be the responsibility of the Treasurer-Manager.

Financial assets will be reported at each regularly scheduled board meeting as part of the financial/management report. The report shall contain information concerning:

- compliance with this policy and regulatory requirements regarding minimum investment quality and maximum investment limits
- dollar volume and yields of investments by investment category
- variances to budget, and historic comparisons

- large investments above a dollar threshold set by board resolution
- particulars of **all** investment transactions made and held since the last board meeting, as required under the Act, section 198(4).

Compliance

Annually, the Audit Committee will ensure compliance with this policy. The Audit Committee is responsible for developing and conducting an annual review of market risk management procedures in place relative to the Market Risk Management policy requirements established above, and will report its findings and recommend any necessary corrective action to the board of directors. The Audit Committee may engage the services of additional volunteers or experts to assist in its review.

The external auditor shall conduct whatever tests are necessary regarding this policy to meet generally accepted auditing standards and shall report any shortfalls to the Audit Committee.

The board will review written correspondence from the Ministry, DICO or designated stabilization authority regarding market risk management matters, and will investigate and respond as appropriate.

Policy Approval and Review

This policy, and any subsequent recommended changes to this policy, must be approved by the board of directors. This policy shall be reviewed annually for ongoing appropriateness by the board (or by a delegated subcommittee of the board).