



INVESTMENT PRACTICES AND INTERNAL CONTROLS MANUAL

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I. INVESTMENT PRACTICES

A. Introduction:

The Board of Directors of Districts Mutual Insurance Company (DMI) has the responsibility of conducting cash and investment transactions for all funds held by or for the benefit of DMI. The Board of Directors shall implement the investment policies by following the investment practices and internal controls herein delineated.

B. Objective

The Investment Practices and Internal Controls Manual provides an outline for investment management. This manual shall be reviewed annually by the Board of Directors.

C. Prudence and Ethical Standards:

The standard of prudence to be used by the Board of Directors shall be the “prudent person” and shall be applied in the context of managing the overall portfolio. DMI’s Board of Directors, or specified person(s) performing the investment functions, acting in accordance with written policies and procedures and exercising due diligence, shall not be responsible for an individual security’s credit risk or market price changes, provided that deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments. The standard of prudence and ethical standards should mirror what are in the investment procedures for DMI.

The “prudent person” standards is herewith understood to mean the following:

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.

D. Investment Decisions:

The Board of Directors shall adhere to the guidelines of DMI’s investment procedures regarding all investment purchases or any other cash and investment transactions.

E. Delegation of Authority:

As established by the By-Laws, the President and Treasurer have authority to transact investments. The Board of Directors shall establish the overall investment policies. The management and implementation may be delegated to such designee/agent as chosen by the Board of Directors who shall establish practices for the operations of the investment program. Such practices shall include explicit written delegation of authority to other investment personnel responsible for investment transactions.

F. Ethics and Conflicts of Interest:

For the protection of the Board members, it is imperative that full written disclosure be made by anyone involved with the investment activity of DMI to DMI of any material interests which they may hold in a financial institution (brokers/dealers, banks, etc.) which conducts business with DMI. This should mirror and reference what is in the Investment Procedures.

Any local, county, or state ethics laws shall also be in force.

G. Segregation of Duties and Compensating Controls

DMI shall establish written internal controls, which should include:

1. Control of Collusion:

Collusion is a situation where two or more individuals are working in conjunction to defraud DMI.

2. Segregation of duties:

By separating the person who authorizes or performs the transaction from the people who record or otherwise account for the transaction, a good separation of duties is achieved.

3. Avoidance of physical delivery of securities:

Book entry securities are much easier to transfer and account for, since actual delivery is never taken. Physical delivery securities must be properly safeguarded, as are any valuable documents. The potential of fraud and loss increases with physical delivery securities. Bearer-form securities are much easier to convert to personal use than securities that are registered in the name of DMI.

4. Clear delegation of authority:

Anyone involved with the investment activities of DMI must have a clear understanding of their authority and responsibilities to avoid any improper actions. Clear delegation of authority also preserves the internal control structure.

5. Written confirmation of all transactions (transfer, fax, internet) for investments and wire transfers:

Due to the potential for errors and improprieties arising from telephone/electronic transactions, they should be documented in writing and approved by the appropriate person.

H. Reporting Requirements:

1. An investment summary report at least quarterly. The report shall contain, but not be limited to, the following information:
 - Rate of return on the portfolio
 - Average days to maturity
 - Monthly portfolio composition
 - Market-to-market valuation
 - Quarterly purchases and sales
2. At a minimum, a semi-annual report shall be presented to the DMI board to update the board on securities held, maturities, investment returns, unrealized gains (losses), comparisons to established benchmarks, market conditions, prevailing investment strategy, and adherence to the Investment Procedures. Securities will be reported on a market-to-market basis.

I. Operations:

1. Practices and duties recommended include:

The accounting provider shall be responsible for providing the Board of Directors with information regarding the cash requirements and required maturity dates. A confirmation form must evidence all security purchases or sales.

Proper documentation and authorization shall be required before any investment transaction is executed.

2. Authorized Electronic Fund Transfers

Only the authorized representatives shall transfer funds according to the approved wire transfer agreements. Transfer instructions and personal identification numbers (PINs) shall be safeguarded.

3. Securities Confirmations

An individual not permitted to purchase and sell investments shall conduct the processing of securities confirmations, including filing and reconciling.

4. Safekeeping Procedures

Certificates of Deposit may be held at the issuing bank.

J. Permissible Assets

	<i>Minimum</i>	<i>Maximum</i>
1. Cash and Short-term	\$500,000	100%

- Commercial paper rated A-1 by Moody’s and/or P-1 by Standard & Poors.
- Pooled short-term money market funds NAIC 1 or 2 rated pools with assets that mature in 365 days or less.
- Certificates of Deposit with maturity dates of 365 days or less.
- Bank repurchase agreements.
- Bankers acceptance.

	<i>Minimum</i>	<i>Maximum</i>
2. Fixed Income	0%	90%

- Securities of the US Treasury.
- Obligations of US states and their subdivisions including: General Obligations, Insured, Special Revenue, and Pre-funded Obligations.
- Preferred stock of US corporations that qualify for amortized cost accounting.
- Dollar denominated notes and bonds of US corporations.
- AAA rated mortgage backed securities – including: pass-throughs, PAC’s, sequentials, accretion directed trances, and Z trances; but excluding such mortgage derivatives as: inverse floaters, interest only strips, principal only strips, and trances labeled support bonds.
- Asset-backed securities rated A or better.
- Commercial mortgage backed securities rated A or better.

	<i>Minimum</i>	<i>Maximum</i>
3. Equities	0%	20%

- Equity securities of US Corporations listed on US exchange recognized by the NAIC/SVO.
- US dollar quoted mutual funds and exchange traded funds listed on US exchange recognized by the NAIC/SVO.

	<i>Minimum</i>	<i>Maximum</i>
4. Other Investments	0%	10%

- Additional authority is granted for investments which are not otherwise authorized by this Policy and which are not specifically prohibited by statute, including that portion of any investments which may exceed the limits of sections 1. to 3. above. The aggregate of all investments made under this section 4. may not exceed five percent (5%) of the Company’s admitted assets, and no single investment may exceed two percent (2%) of admitted assets.

II. INTERNAL CONTROLS

A. Control of Collusion

Investment activity shall occur at the approval of the Board of Directors. Written minutes of Board meetings and significant actions taken shall be maintained. Board meetings are typically held quarterly. An investment schedule will be reviewed as part of the quarterly agenda.

B. Segregation of Duties

To maintain an appropriate segregation of duties, the following activities are designated by position:

Board President or Designee/Agent:	Execution of investment purchase or sale
Executive Vice President:	Transfer of cash between funds
Accountant:	Accounting for transactions in general ledger and preparation of quarterly investment schedule

Occasionally it may be necessary for one person to perform two of the above activities, but in no case would one individual do all three functions.

C. Written Confirmation of Transactions

All investment transactions must be documented in written form. Confirmation of all security purchases, calls, or sales must be in written format (including e-mail documentation). Written confirmation will be verified against monthly investment reports for reconciliation and verification of completeness. Written confirmations shall be maintained for a minimum of three years from the transaction date.