



# City of Richmond

## Report to Committee

**To:** Finance Committee **Date:** February 9, 2022  
**From:** Ivy Wong **File:** 03-0900-01/2022-Vol  
 Acting Director, Finance 01  
**Re:** Referral Response – Investment Policy and Portfolio Review

### Staff Recommendation

1. That the staff report titled “Referral Response – Investment Policy and Portfolio Review” dated February 9, 2022 from the Acting Director, Finance be received for information.
2. That staff be directed to conduct the required review and assessment in order to facilitate Council in considering the MFA Long-Term Diversified Multi-Asset Class Fund.

Ivy Wong  
 Acting Director, Finance  
 (604-276-4046)

| REPORT CONCURRENCE                                        |                                                               |                                                              |
|-----------------------------------------------------------|---------------------------------------------------------------|--------------------------------------------------------------|
| <b>ROUTED TO:</b><br><br>Sustainability & District Energy | <b>CONCURRENCE</b><br><br><input checked="" type="checkbox"/> | <b>CONCURRENCE OF GENERAL MANAGER</b><br><br>Acting GM, F&CS |
| <b>SENIOR STAFF REPORT REVIEW</b>                         | <b>INITIALS:</b><br>                                          | <b>APPROVED BY CAO</b><br>                                   |

## Staff Report

### Origin

At the February 3, 2020 General Purposes Committee, discussion ensued concerning whether or not the City's investments in some specific Canadian Chartered Banks were socially responsible investments. Council passed the following referral motion:

*That staff review the City's investment policy and portfolio and report back on recommendations.*

This report supports Council's Strategic Plan 2018-2022 Strategy #5 Sound Financial Management:

*Accountable, transparent, and responsible financial management that supports the needs of the community into the future.*

*5.1 Maintain a strong and robust financial position.*

*5.3 Decision-making focuses on sustainability and considers circular economic principles.*

### Findings of Facts

Socially Responsible Investing (SRI) has gained significant momentum and attention in the past decade as investors, portfolio managers and policy makers are working collaboratively in supporting the reform and implementation of a more sustainable global financial system. SRI approach was once an exception, now it is becoming the norm.

The United Nations Principles for Responsible Investment (PRI) is the world's leading proponent of responsible investment that supports its international network of investor signatories in incorporating Environmental, Social and Governance (ESG) factors into their investment and ownership decisions. Table 1 provides an overview of the PRI's framework:

| <br>ENVIRONMENTAL                                                      | <br>SOCIAL                                                                            | <br>GOVERNANCE                                                                                                        |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"><li>■ climate change</li><li>■ resource depletion</li><li>■ waste</li><li>■ pollution</li><li>■ deforestation</li></ul> | <ul style="list-style-type: none"><li>■ human rights</li><li>■ modern slavery</li><li>■ child labour</li><li>■ working conditions</li><li>■ employee relations</li></ul> | <ul style="list-style-type: none"><li>■ bribery and corruption</li><li>■ executive pay</li><li>■ board diversity and structure</li><li>■ political lobbying and donations</li><li>■ tax strategy</li></ul> |

Table 1: PRI's ESG Framework (Source: PRI)

## Analysis

### Independent ESG Review of the City's Investment Portfolio

The City engaged an independent firm to review and assess its investment portfolio's ESG rating. Morgan Stanley Capital International (MSCI) is one of the largest global investment research firms that provides benchmark indices and analytical services to investors. MSCI provides ESG Rating reports to measure a company's resilience to long-term, industry-specific environmental, social and governance (ESG) risks. Issuers are rated on a scale from "AAA" to "CCC" according to their exposure to industry-specific ESG risks and their ability to manage those risks relative to their peers.

The MSCI ESG Rating for the City's December 31, 2021 investment portfolio holdings was determined to be very high at AA (Table 2).

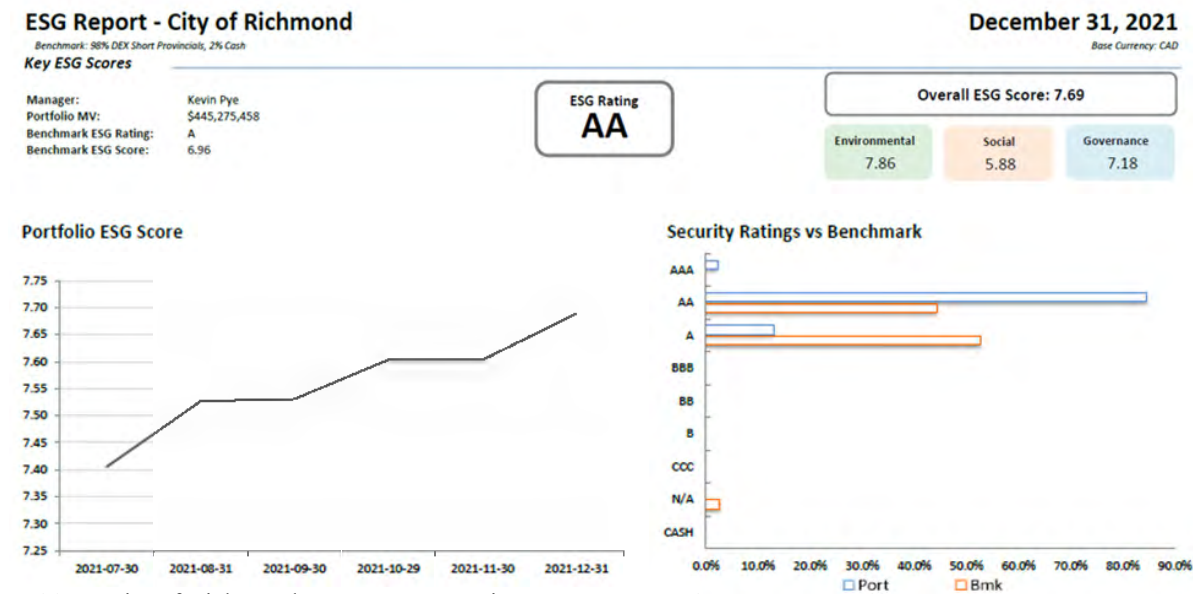


Table 2: City of Richmond's MSCI ESG Rating Report (December 31, 2021)

Some of the factors that contribute to this high ranking include the fact that the City's investment partners are all PRI signatories that follow the UN PRI framework, where ESG considerations, practices and disclosures are incorporated into all investment decisions and processes. The issuers of the City's investments are also required to produce annual disclosures of their corporate accountability and an ESG Report. The majority of the City's investments are in governments and banks, which make up a significant portion of the top holdings of various global ESG indices and ESG funds due to their positive ESG characteristics.

### Continued Global Movement to a Standardized ESG Disclosures Framework

There is a growing demand for improved disclosure of sustainability and ESG information. A multitude of sustainability reporting standards already exist, such as the Global Reporting Initiative (GRI), the Task Force on Climate-related Financial Disclosures (TCFD) and the Sustainability Accounting Standards Board (SASB). The different frameworks and standards have led to confusion and inconsistent disclosure in the market.

At the 26th United Nations Climate Change Conference that took place in November 2021, a new International Sustainability Standards Board (ISSB) was announced in order to respond to a much-needed consistent approach at a global level. The purpose of the ISSB is to address the disparities in the guidance and frameworks on ESG reporting. A Canadian Sustainability Standards Board will also liaise with the new ISSB to provide Canadian investors with a standardized approach that will guide companies on what sustainability disclosures are required to supplement their financial statements.

### Review of City's Investment Policy 3703

The City's Investment Policy 3703 (Attachment 1) prescribes the fundamental investment objectives that guide the City's investment activities. In the order of importance, the four investment objectives are:

- (i) Adhering to statutory requirements,
- (ii) Maintaining safety of capital,
- (iii) Providing liquidity of investment, and
- (iv) Maximizing possible investment yield after considering the first three objectives.

In supporting the City's commitment in advancing Richmond's climate leadership role, there is opportunity for an additional investment objective to be added to the City's Investment Policy once the ESG standardization becomes mature and recognized. When an industry-accepted ESG standard becomes available, the City will be able to establish a more objective and comprehensive investment mandate in achieving the desired balance between risks, social value creation and financial returns.

Staff will continue to monitor the development of the ESG reporting landscape and will present future amendment to the City's Investment Policy on ESG integration when the standardization of industry-approved ESG definitions, reports and disclosures become established.

### Expanding ESG-Integrated Investment Options through the Municipal Finance Authority (MFA)

Under the *Community Charter*, local governments are permitted to invest in pooled investment funds under section 16 of the *Municipal Finance Authority Act*. The MFA understands local governments' needs and it believes that investment processes that incorporate ESG factors and other broad systemic issue can lead to better investment outcome.

Currently, the MFA offers the following products and pooled investment funds to its members:

- Pooled High Interest Savings Account
- Money Market Fund
- Government-Focused Ultra-Short Bond Fund
- Short-Term Bond Fund
- Fossil Fuel Free Short-Term Bond Fund
- Mortgage Fund
- Diversified Multi-Asset Class Fund (DMAC Fund) – New in January 2022

Under the City’s Investment Policy, the City could invest up to 20% of the investment balance in the MFA Pooled Investment Funds. The City is currently not participating in any of the MFA Pooled Investment Funds because, with the exception of the new DMAC Fund, all other available MFA products and pooled funds are similar to the holdings of the City’s self-directed investment portfolio.

*The DMAC Fund*

The MFA, through collaboration with local government finance professionals and MFA’s Trustees, created the new managed DMAC Fund as a low-carbon long-term investment option for local governments. As summarized in Table 3 below, the DMAC Fund offers a broad diversification and asset mix, namely by the inclusion of a diversified range of equity and alternative securities that are otherwise not permissible municipal investments under the existing legislation.

| Fund Attributes                | Description                                                                                                                                                                                                                                                                                                                                                                                                                                   |
|--------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Fund Manager                   | Phillips, Hager & North Investment Management                                                                                                                                                                                                                                                                                                                                                                                                 |
| Fund Description               | A diversified portfolio of global financial asset classes that is structured to provide long-term asset growth over a 10-year or longer time horizon.                                                                                                                                                                                                                                                                                         |
| Fund Objective                 | The primary purpose of the Fund is to invest capital over the long-term to grow at a rate that exceeds inflation, while minimizing risk through asset class selection and diversification.                                                                                                                                                                                                                                                    |
| Investment Limit               | Maximum investment limit of 25% of a municipality’s eligible reserves for municipalities with a population greater than 10,000 residents.                                                                                                                                                                                                                                                                                                     |
| Asset Diversification          | The Fund generally invests in low volatility assets, e.g. global and Canadian equities, bonds, mortgages, infrastructure debt and real estate etc.                                                                                                                                                                                                                                                                                            |
| Fund Return                    | The Fund aims to provide risk-adjusted real returns of 3.5% annually in the long-term.                                                                                                                                                                                                                                                                                                                                                        |
| Pre-Qualification Requirements | Due to the long-term nature of the Fund, participation in the Fund will require:<br>(i) Local municipalities to update their Investment Policy to include a policy statement regarding provision for monies not needed for 10 years or longer to be eligible under the MFA long-term pooled investment fund, and<br>(ii) Council to provide acknowledgement of designated specific reserves earmarked for such approved long-term investment. |
| ESG Integration                | The Fund is managed under the United Nations Principals for Responsible Investing (UN PRI) ESG framework.<br><br>The Fund will be a low carbon fund with a significant portion of the asset classes employing a strict Fossil Fuel Free screen. The Fund is not designed to be a fully Fossil-Fuel-Free investment portfolio.                                                                                                                 |
| Fees                           | 0.33%                                                                                                                                                                                                                                                                                                                                                                                                                                         |

Table 3: Key Features of the MFA DMAC Pooled Investment Fund

Staff believe that the new DMAC fund would provide opportunities for increased asset diversification and enhanced investment returns that are unavailable through the City's self-directed permitted investments under the *Community Charter*. It is recommended that Council provide direction to staff to perform the required due diligence in order to facilitate Council in considering the long-term DMAC Fund. If endorsed, staff will report back with recommendations to Council for future consideration.

**Financial Impact**

None.

**Conclusion**

The referral response on the City's investment policy and portfolio review be received for information and the MFA DMAC Fund be introduced to Council for further consideration.



Venus Ngan  
Manager, Treasury and Financial Services  
(604-276-4217)

Attachment 1: City's Investment Policy 3703



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## POLICY 3703:

It is Council policy that:

### 1. POLICY

The purpose of this policy is to ensure that the City's practices and procedures in the investment of public funds are in compliance with statutory requirements of the *Community Charter*, while ensuring safety of capital, maintaining appropriate liquidity in meeting anticipated cash flow demands, and attaining a reasonable rate of return after taking into account the investment constraints and liquidity requirements.

### 2. OBJECTIVES

Conservative management philosophy is followed in investment activities of all public funds held by the municipality. Four fundamental objectives, in priority order, are as follows:

#### (i) Adherence to Statutory Requirements

Authority for investment guidelines of municipal funds is provided in section 183 of the *Community Charter*.

#### (ii) Safety of Capital

Investment activities will be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. Preservation of capital will be accomplished through:

- Diversification, as outlined in section 9, and
- Risk control, whereby portfolio components are limited to conservative types of investments as defined in section 8.

#### (iii) Liquidity of Investment

The investment portfolio will be administered to ensure adequate cash flow is available to meet all reasonably anticipated operating and capital requirements.

#### (iv) Return on Investment

The investment portfolio will be designed with the objective of maximizing the rate of return through budgetary and economic cycles, taking into account the investment constraints and liquidity requirements. The Financial Officer will take into account these constraints and objectives in the selection of investments to be included in the City's portfolio. The portfolio will be structured to attain optimum performance results as directed by the Policy, and to create maximum value to the City, net of any costs incurred in the investment process.



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### 3. PRUDENCE

Investments will be made with judgement and care, under circumstances then prevailing, by persons of prudence, discretion and intelligence exercised in the management of other people's affairs, not for speculation, but for investment, considering the probable safety of capital as well as the probable income to be derived. Where external managers are engaged to perform trading activity, the external managers will be required to exercise the degree of care, diligence, and skill which a prudent investment counsel would exercise in similar circumstances. The Financial Officer acting in accordance with this policy and exercising due diligence will be relieved of personal responsibility for an individual security's credit risk or market price changes.

### 4. AUTHORIZATION

Authority to manage the City's investment program is derived from section 149 of the *Community Charter*, as follows:

"Financial Officer

One of the municipal officer positions must be assigned the responsibility of financial administration, which includes the following powers, duties and functions:

- a) receiving all money paid to the municipality;
- b) ensuring the keeping of all funds and securities of the municipality;
- c) investing municipal funds, until required, in authorized investments;
- d) expending municipal money in the manner authorized by the council;
- e) ensuring that accurate records and full accounts of the financial affairs of the municipality are prepared, maintained and kept safe;
- f) exercising control and supervision over all other financial affairs of the municipality."

The Financial Officer is the portfolio administrator and has the ultimate responsibility for the prudent investment of the portfolio. The Financial Officer may retain a professional investment manager(s) ("Investment Manager(s)") to provide investment advice and carry out the instructions of the Financial Officer.

The Financial Officer will:

- administer the Policy;
- review the Policy annually, which will include a reassessment of the fund's objectives, the benchmark portfolio and the impact of any changes in liquidity requirements if necessary;
- select the Investment Manager(s) and City's custodial bank;
- regularly review the quantitative and qualitative performance of the Investment Manager(s) including an evaluation of the rates of return, an analysis of the areas where the Investment Manager(s) added or reduced value, and a review of the Investment Manager(s) in the context of the criteria for their selection;





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- be responsible for regularly monitoring the asset mix of the portfolio and taking the action necessary, to correct any breaches of applicable legislation or the permitted asset mix ranges set out in this Policy;
- provide information on significant cash flow changes to the Investment Manager(s);
- be responsible for the oversight of any professional Investment Manager(s).
- have the authority to appoint and terminate the Investment Manager(s).

The Investment Manager(s) will:

- provide the Financial Officer with monthly reports of actual portfolio holdings, detailing each class of assets and how they conform to policy maximums as defined in section 8 and 9;
- present to the Financial Officer a quarterly review of investment performance, including an explanation of any shortfalls of their investment results compared to the investment objectives;
- provide estimates of future returns on investments and review proposed investment strategies that may be used to meet the objectives;
- attend a meeting with the Financial Officer at least once each year to review the results they have achieved;
- inform the Financial Officer promptly of any element of the Policy that could prevent attainment of the Plan's objectives;
- give prompt notice to the City's custodial bank of all purchases and sales of securities;
- report all investment transactions quarterly to the Financial Officer;
- provide the Financial Officer with a quarterly certificate of compliance with the Policy for the quarter just ended.

## 5. ETHICS AND CONFLICT OF INTEREST

The Investment Manager(s), Financial Officer and any individuals involved in the investment process will refrain from personal business activity that could conflict with the proper execution of the investment program or impair ability to make unbiased investment decisions. Parties will disclose any material personal financial interest in investments involved or in financial institutions that conduct business with the City. Any deviation is to be reported to the City Solicitor immediately.

## 6. IMPLEMENTATION

An active or passive investment style may be adopted, depending on suitability of each in meeting the City's investment objectives.



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**7. AUTHORIZED INVESTMENT DEALERS AND INSTITUTIONS**

The Investment Manager(s) will be registered with a regulated securities commission. They will be responsible for maintaining a list of approved financial institutions and brokers/dealers authorized to provide investment services. An annual review of this list will be completed by the Investment Manager(s), whereupon, the recommendations for any additions and deletions will be discussed and approved by the Financial Officer.

**8. PERMITTED INVESTMENTS**

Under the *Community Charter* Section 183, a municipality may invest money that is not immediately required in one or more of the following:

- a) securities of the Municipal Finance Authority;
- b) pooled investment funds under section 16 of the Municipal Finance Authority Act;
- c) securities of Canada or of a province;
- d) securities guaranteed for principal and interest by Canada or by a province;
- e) securities of a municipality, regional district or greater board;
- f) investments guaranteed by a chartered bank;
- g) deposits in a savings institution, or non-equity or membership shares of a credit union;
- h) other investments specifically authorized under this or another Act.

The following table sets out the City's permitted investments, minimum credit rating requirements and their limits:

| Asset Class                                             | Dominion Bond rating services limited (DBRS) <sup>1</sup><br>Short Term / Long Term Rating | Limits per issuer<br>(as a % of total portfolio) |
|---------------------------------------------------------|--------------------------------------------------------------------------------------------|--------------------------------------------------|
| <b>Federal Issuers</b>                                  |                                                                                            |                                                  |
| Securities issued or backed by the Government of Canada | No minimum requirement                                                                     | No limit                                         |
| <b>PROVINCIAL ISSUERS</b>                               |                                                                                            |                                                  |
| All Provinces                                           | R-1 (high) / AAA, AA (high), AA                                                            | 25% per province                                 |
| All Provinces                                           | R-1 (middle) / AA (low)                                                                    | 20% per province                                 |
| All Provinces                                           | R-1 (middle) / A (high)                                                                    | 10% per province                                 |
| All Provinces                                           | R-1 (low) / A, A (low)                                                                     | 5% per province                                  |
| <b>TOTAL PROVINCES</b>                                  |                                                                                            | Maximum 50%                                      |
| <b>Chartered Banks</b>                                  |                                                                                            |                                                  |
| Schedule I, II & III banks                              | R-1 (high) /AAA, AA                                                                        | 15 % per bank                                    |
| Schedule I, II & III banks                              | R-1 (middle) /AA, AA (low)                                                                 | 10 % per bank                                    |
| Schedule I, II & III banks                              | R-1 (middle) / A (high)                                                                    | 5 % per bank                                     |
| Schedule I, II & III banks                              | R-1 (low) / A (low)                                                                        | 3 % per bank                                     |
| <b>TOTAL CHARTERED BANKS</b>                            |                                                                                            | Maximum 50%                                      |



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| B.C. credit unions                                                                                                                        |                                                                                                                  |
|-------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------|
| Credit unions with total assets <sup>2</sup> more than \$10 billion                                                                       | The greater of:<br>(i) 10% of total portfolio balance per credit union, or<br>(ii) \$75 million per credit union |
| Credit unions with total assets <sup>2</sup> between \$500 million and \$10 billion                                                       | The greater of:<br>(i) 5% of total portfolio balance per credit union, or<br>(ii) \$50 million per credit union  |
| Federal credit unions                                                                                                                     |                                                                                                                  |
| Deposit term cannot exceed 1 year if long-term DBRS credit rating of A (low) is not attained <sup>3</sup>                                 |                                                                                                                  |
| Federal credit unions with:<br>• Long-term DBRS credit rating under A (low); and<br>• Short-term DBRS credit rating higher than R-1 (low) | The greater of:<br>(i) 5% of total portfolio balance per credit union, or<br>(ii) \$50 million per credit union  |
| Federal credit unions with:<br>• Long-term DBRS credit rating under A (low); and<br>• Short-term DBRS credit rating R-1 (low)             | The greater of:<br>(i) 3% of total portfolio balance per credit union, or<br>(ii) \$30 million per credit union  |
| <b>TOTAL CREDIT UNIONS</b>                                                                                                                | Maximum 30%                                                                                                      |
| Pooled Investments                                                                                                                        |                                                                                                                  |
| Pooled funds                                                                                                                              | Maximum 20%                                                                                                      |
| OTHER SECURITIES                                                                                                                          |                                                                                                                  |
| Municipality, Regional District or Greater Board                                                                                          | Maximum 10%                                                                                                      |

<sup>1</sup> If DBRS credit rating is not available, the City can use an equivalent credit rating provided by an approved credit rating organization such as Standard & Poor's Corporation (S&P) and Moody's Investors Services Inc. (Moody's)

<sup>2</sup> Based on latest audited financial statements

<sup>3</sup> Federal credit union that has long-term DBRS credit rating A (low) or higher will follow the equivalent per issuer limits under the Chartered Bank section for its long-term and short-term investments, where the total investments in all credit unions cannot exceed a combined total of 30% of the City's investment portfolio.

## 9. DIVERSIFICATION

The City recognizes that prudence in investment selection is essential to minimize interest rate and credit risk.

- Interest Rate Risk – At each interim and annual reporting periods, the Investment Manager(s) will monitor the performance of the cash and bond components of the portfolio against the selected benchmarks. The Investment Manager(s) will also assess the duration of the bond components of the portfolio to ensure they fall within a year and a half of the duration of the benchmark against which bond performance is measured. The 91-Day T-Bill Index will be the basis for benchmarking the cash component of the portfolio. For the bond components of the portfolio, the indices within the FTSE Canada Bond Index, or its equivalent prevailing index as amended from time-to-time by the provider of the benchmarks, will be selected as the benchmarks. Selection of the appropriate benchmark for each bond component will



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be based on the index with the duration closest to the duration of the bond component being evaluated. The following indices fall within the FTSE Canada Universe Bond Index:

- FTSE Canada Universe All Government Index
- FTSE Canada Short Term All Government Index
- FTSE Canada Mid Term All Government Index
- FTSE Canada Short/Mid All Government Index
- FTSE Canada Long Term All Government Index

- Credit Risk – The Investment Manager(s) will minimize credit risk by investing in conservative types of instruments. A minimum of 90% of the portfolio's market value is required to carry a DBRS credit rating of A (high) or higher or the equivalent R1-middle or higher.

Diversification will be achieved through:

- Setting limits on the amount of investments with a specific maturity, from a specific issuer or a specific sector;
- Investing the targeted amount of assets in liquid investments to ensure funds are readily available; and
- Selecting assets with varying maturity terms.

In addition, the Investment Manager(s) will engage in the rebalancing of the portfolio to adhere to parameters as defined in this policy or any addendums agreed upon by the Financial Officer and the Investment Manager(s).

## 10. COMPETITIVE BIDS

The Financial Officer or Investment Manager(s) will solicit competitive verbal quotations for the purchase and sale of securities when it is prudent to do so. This policy recognizes that, from time to time, offerings of value may require immediate action. Under such circumstances competitive bids may not be sought provided that value can be substantiated by market data.

## 11. SAFEKEEPING AND CUSTODY

All transactions will be executed by the delivery-versus-payment basis to ensure securities are deposited in an eligible financial institution with the release of funds. Settlement will take place at the main branch of the City's custodial bank in any Canadian city. Securities will be held by the City's custodial bank or alternatively, will be registered with the Central Depository for Securities (CDS).

- **Authorization:** The custodial bank will not accept delivery or payment without prior authorization and instructions for the City.



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- **Evidence:** All transactions traded in-house will be evidenced by a contract advice from the investment dealer, as well as a settlement advice from the custodial bank.
- **Registration:** All securities that are in registerable form will be registered in the name of the City of Richmond.
- **Repurchase Agreements:** In addition to all the terms and conditions above, the City's custodial bank will be responsible for ensuring that the repurchase agreement for overnight transactions has been duly executed.

## 12. INTERNAL CONTROLS

External audits will be performed annually, including an assessment of investment effectiveness and risk management.

## 13. PERFORMANCE STANDARDS

The investment portfolio will be designed to obtain an above market benchmark, taking into account the City's investment risk constraints, cash flow requirements, and active management strategy. This policy recognizes that the reliability of performance evaluation (i.e. comparison to benchmarks) increases with the duration of the measurement period.

## 14. REPORTING

The Financial Officer will prepare an investment report on a quarterly basis to Council. The report will provide a summary of the securities held at the end of the reporting period including issuer diversification and market values.

The Investment Manager(s) will conduct at each quarter end a review of the portfolio, including strategy employed, duration, liquidity, and a forecast of upcoming market conditions.

## 15. ADOPTION AND REVIEW

The policy will be reviewed annually by the Financial Officer, and any suggested modifications will be presented to Council for adoption.