



To: Finance Committee

Date: May 21, 2009

From: Jerry Chong
Director, Finance

File: 03-0900-01/2008-Vol 01

Re: Investment Policy Update

Staff Recommendation

That Council Policy 3703 (Investment Policy) adopted by Council on June 25, 2007 be amended by deleting Sections 8 and 9 and replacing them with the proposed Sections 8 and 9 as outlined in Attachment 2 of the staff report dated May 21, 2009 from the Manager, Treasury.

Jerry Chong
Director, Finance
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ROUTED TO:	CONCURRENCE	CONCURRENCE OF GENERAL MANAGER	
Law.....	Y <input checked="" type="checkbox"/> N <input type="checkbox"/>	<i>Amal</i>	
REVIEWED BY TAG	YES <input checked="" type="checkbox"/> NO <input type="checkbox"/>	REVIEWED BY CAO <i>Acting</i>	YES <input checked="" type="checkbox"/> NO <input type="checkbox"/>

Staff Report

Origin

Investment Policy 3703 was last amended and approved by Council on June 25, 2007. The Investment Policy is to be reviewed annually and be revised on an as-necessary basis to ensure that the investment objectives are being met.

Staff reviewed the current Investment Policy and identified opportunities for amendments.

Analysis

The current Investment Policy includes dollar limits with approved security issuers and financial institutions. When these limits were initially established, the City's investment portfolio had an average balance of approximately \$300 million. As the City's investment portfolio continues to increase (current portfolio level is at over \$500 million), the dollar limits originally established have created restrictions that would hinder effective investment strategies to be deployed.

The City conducted a review of the current Investment Policy. From the review, it is recommended that:

- The current "dollar limits" be changed to "percentage of portfolio limits"; and
- The allowable mix for each asset class be reviewed to realign the risk exposure of our portfolio mix with the current economic conditions.

The recommended changes above allow the investment limits to vary as the size of the City's investment portfolio changes. The recommendations also enable the City to better diversify risks by investing with security issuers that provide the most favourable rate of return, while operating within the legislated parameters of section 183 of the Community Charter.

Recommended Changes

Section 8 – Permitted Investment

- The limit for each asset class has been modified from a "dollar limit" to a "percentage limit", where a consistent percentage limit per issuer has been applied to all securities issuers (see Table 1).
- The "limits per issue" restriction has been removed and replaced with "limits per issuer". The limit per issuer provides a better measurement of risk exposure of our portfolio holdings.
- The policy has been revised to more explicitly express Dominion Bond Rating Service (DBRS) as the credit agency used for evaluating credit ratings. Wordings have been changed to take into account both long-term and short-term DBRS ratings.

Table 1: Amended Limits Per Issuer

Type of Issuer	DBRS Short-Term / Long-Term Rating	Limits Per Issuer (% of total portfolio)
Provincial	R-1 (high) / AAA	25% per province
Provincial	R-1 (middle) / AA	20% per province
Provincial	R-1 (low) / A	10% per province (with exception of 5% for PEI and Newfoundland)
Schedule I, II & III Banks	R-1 (high) / AAA	10% per bank
Schedule I, II & III Banks	R-1 (middle) / AA	5% per bank
Schedule I, II & III Banks	R-1 (low) / A	3% per bank

Note: For comparison of the amended limits with the current limits, refer to Table 2 in page 5 of this report.

Section 9 – Diversification

- The minimum and maximum for federal, provincial, and schedule I, II, & III banks have been superseded by the new percentage limits in section 8. The amended percentage limits (as a percentage of total portfolio balance) are determined based on their credit ratings.
- Some of these changes in the limits include the following (See Table 2 for a comparison of the existing and the proposed investment limits):

Federal Issuers

- No change. The total limit for federal issues (all backed by the Government of Canada) remains at a minimum of 25% and up to a maximum of 75%.

Provincial Issuers

- The upper limit for AAA provincial issuers remains at 25%.
- Instead of the existing upper limit of 25%, the percentage limits for provincial issuers with AA and A DBRS ratings have been lowered to 20% and 10% respectively, with the exception of 5% for PEI and Newfoundland.
- The total limit for provincial issues remains at a minimum of 15% and up to a maximum of 50% of total portfolio balance.

Chartered Banks

- The upper limit for AAA bank issuers remains at 10%.
- Instead of the existing upper limit of 10%, the percentage limits for Schedule I, II and III bank issuers with AA and A DBRS ratings have been lowered to 5% and 3% respectively.
- To reduce the risk exposure in the banking sector, the total investment limit of all Schedule I, II & III banks has decreased from a maximum of 50% to 25% of total portfolio balance.

Credit Unions

- In November 2008, the Provincial legislature passed amendments to the Financial Institutions Act to provide unlimited deposit insurance protection on all deposits in British Columbia's credit unions.
- As a result of unlimited deposit insurance protection:
 - The maximum limit for each credit union has increased from \$25 million to the greater of \$30 million or 5% of the total investment portfolio;
 - The limit on total investment in credit unions has increased from \$60 million to the greater of \$75 million or 10% of the total portfolio balance; and
 - The restriction over the term of the deposits being held at credit unions has been extended from 90 days to 1 year.

Pooled Investments

- Pooled investment fund will continue to be capped at 20% of total portfolio.

Other Securities

- New investment limits have been introduced for securities of a municipality, regional district or greater board with an upper limit of 10% per issuer.

Refer to Attachment 1 for a copy of the current Investment Policy 3703.

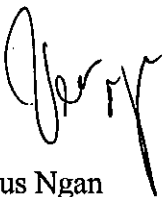
Refer to Attachment 2 for the proposed Sections 8 and 9 of Investment Policy 3703.

Financial Impact

None.

Conclusion

The proposed amendments to sections 8 and 9 of Investment Policy 3703 be adopted by Council.



Venus Ngan
Manager, Treasury
VN:vn

Table 2: Comparison of Current and Proposed Investment Limits

ASSET CLASS	LONG TERM RATING	CURRENT LIMITS PER ISSUE / LIMITS PER ASSET CLASS	PROPOSED LIMITS PER ISSUER (as a % of total portfolio)
FEDERAL ISSUERS			
Federal & Federally guaranteed	AAA	\$100 m / 75% (min 25%)	75% (min 25%)
PROVINCIAL ISSUERS (includes provincial government and provincial crown corporations)			
Alberta	AAA	\$70 m / 25%	25% per province
Province of BC & Prov. BC guaranteed	AA	\$50 m / 25%	20% per province
Ontario	AA	\$50 m / 25%	20% per province
Saskatchewan	AA	\$50 m / 25%	20% per province
Manitoba	A	\$30 m / 25%	10% per province
New Brunswick	A	\$30 m / 25%	10% per province
Quebec	A	\$30 m / 25%	10% per province
Nova Scotia	A	\$30 m / 25%	10% per province
Newfoundland and Labrador	A	\$30 m / 5%	5% per province
Prince Edward Island	A	\$30 m / 5%	5% per province
TOTAL PROVINCES		\$300 m / 50%	50% (min 15%)
CHARTERED BANKS			
Schedule I, II & III banks	AAA	\$50 m / 10% per bank	10% per bank
Schedule I, II & III banks	AA	\$50 m / 10% per bank	5% per bank
Schedule I, II & III banks	A	\$30 m / 10% per bank	3% per bank
TOTAL SCHEDULE I, II & III BANKS		\$300 m / 50%	25% (min 0%)
CREDIT UNIONS (credit unions terms are revised to a limit of 1 year)*			
VanCity		\$25 m	The greater of: i) 5% of total portfolio balance per credit union, or ii) \$30 million per credit union
Coast Capital		\$25 m	
BC Central Credit Union		\$25 m	
Other Credit Unions		\$25 m	
TOTAL CREDIT UNIONS		\$60 m	The greater of: i) 10% of total portfolio balance, or ii) \$75 million (min 0%)
POOLED INVESTMENTS			
Pooled funds		\$150 m total	20% (min 0%)
OTHER SECURITIES			
Municipality, Regional District or Greater Board		--	10% (min 0%)

* 90 days under current Investment Policy 3703

**POLICY 3703:****1. POLICY**

The purpose of this investment policy is to establish and maintain practices and procedures to invest public funds with the highest return on investment and with the maximum security and appropriate liquidity while meeting daily cash flow demands and conforming to all legislation governing the investment of public funds. This policy applies to the investment activities of the General, Water, Sewer, Capital, Trust and Reserve Funds.

2. OBJECTIVES

The primary objectives of investment activities will be adherence to statutory requirements, safety, liquidity and return on investment.

- **Statutory Requirements:** Authority for investment guidelines of municipal funds is provided in section 183 of the Community Charter.
- **Safety:** Investments 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 paragraph 9, and
 - Risk control, whereby portfolio components are limited to safer types of investments as defined in paragraph 8.
- **Liquidity:** The investment portfolio will be administered to ensure adequate cash flow is available to meet all reasonably anticipated operating requirements.
- **Return on Investment:** The investment portfolio will be designed with the objective of maximizing the rate of return through budgetary and economic cycles. 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.

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.



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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;
- 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;



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- 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.

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."



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Potential investments may include the following:

Asset Class	DBRS Ratings	Long Term	Limits per issue
Federal & Federally guaranteed	R-1 high	AAA	\$100m
Province of BC & Province of BC guaranteed	R-1 high	AA	\$50m
Alberta	R-1 high	AAA	\$70m
Ontario	R-1 high	AA	\$50m
All other provinces		AAA	\$70m
All other provinces		AA	\$50m
All other provinces		A	\$30m
TOTAL PROVINCES (incl BC)			\$300m
Schedule I & II & III banks		AAA	\$50m/bank
Schedule I & II & III banks		AA	\$50m bank
Schedule I & II & III banks		A	\$30m bank
Total Schedule I & II & III banks			\$300m
Pooled funds			\$150m in total
Except for VanCity, credit unions terms are limited to a period of 90 days.			
VanCity			\$25m
Coast Capital			\$25m
BC Central Credit Union			\$25m
Other Credit Unions			\$25m
Total Credit Unions			\$60m



9. DIVERSIFICATION

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

- Interest Rate Risk – The Investment Manager(s) will monitor the duration of the bond portfolio to ensure it falls within a year and a half of the duration of the benchmark against which bond performance is measured. This assessment will be conducted at interim and annual reporting periods.
- Credit Risk – The Investment Manager(s) will minimize credit risk by investing in safer type of instruments. A minimum of 90% of the portfolio's market value is required to carry a credit rating of AA 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;
- selecting assets with varying maturity terms.

In addition, the Investment Manager(s) will engage in the rebalancing of the portfolio to adhere to parameters defined below.

Asset Class	Minimum	Target	Maximum	Benchmark
Cash & Equivalents	10%	35%	45%	Scotia Capital 91 day T-Bill index
Bonds	55%	65%	90%	Matched to one of the indices falling under the Scotia Capital Domestic Bond Government Index.

Asset Class	Minimum	Maximum
Federal & Federally guaranteed	25%	75%
Province of BC	0%	25%
Alberta	0%	25%
Ontario	0%	25%
Manitoba	0%	25%



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New Brunswick	0%	25%
Nova Scotia	0%	25%
Quebec	0%	25%
Saskatchewan	0%	25%
Newfoundland	0%	5%
Prince Edward Island	0%	5%
TOTAL PROVINCES (and guaranteed)	15%	50%
Schedule I, II & III banks	0%	10%
Total Schedule I, II & III banks	0%	50%
Pooled funds	0%	20%

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.
- **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.



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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.

Below are the proposed Section 8 and Section 9 of Investment Policy 3703:

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	DBRS Short Term / Long Term	LIMITS PER ISSUER (as a % of total portfolio)
FEDERAL ISSUERS		
Federal & Federally guaranteed	R-1 (high) / AAA	75% (min 25%)
PROVINCIAL ISSUERS (includes provincial government, provincial crown corporations, and provincially guaranteed)		
All Provinces	R-1 (high) / AAA	25% per province
All Provinces	R-1 (middle) / AA	20% per province
All Provinces (Except Newfoundland and Prince Edward Island)	R-1 (low) / A	10% per province
Newfoundland and Prince Edward Island	R-1 (low) / A	5% per province
TOTAL PROVINCES		50% (min 15%)
CHARTERED BANKS		
Schedule I, II & III banks	R-1 (high) / AAA	10 % per bank
Schedule I, II & III banks	R-1 (middle) / AA	5 % per bank
Schedule I, II & III banks	R-1 (low) / A	3 % per bank
TOTAL SCHEDULE I, II & III BANKS		25% (min 0%)
CREDIT UNIONS (credit unions terms are limited to a period of 1 year)		
VanCity		The greater of: i) 5% of total portfolio balance per credit union, or ii) \$30 million per credit union
Coast Capital		
BC Central Credit Union		
Other Credit Unions		
TOTAL CREDIT UNIONS		The greater of: i) 10% of total portfolio balance, or ii) \$75 million (min 0%)
POOLED INVESTMENTS		
Pooled funds		20% (min 0%)
OTHER SECURITIES		
Municipality, Regional District or Greater Board		10% (min 0%)

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 DEX Universe Bond Index will be selected as the benchmarks. Selection of the appropriate benchmark for each bond component will be based on the index with the duration closest to the duration of the bond component being evaluated. The following indices fall within the DEX Universe Bond Index:

- DEX Universe All Government Index
- DEX Short Term All Government Index
- DEX Mid Term All Government Index
- DEX Short/Mid All Government Index
- DEX Long Term All Government Index

- Credit Risk – The Investment Manager(s) will minimize credit risk by investing in safer type of instruments. A minimum of 90% of the portfolio's market value is required to carry a DBRS credit rating of AA 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).