



CITY OF HAMILTON
CORPORATE SERVICES DEPARTMENT
Financial Planning, Administration and Policy Division

TO:	Chair and Members Audit, Finance and Administration Committee
COMMITTEE DATE:	December 5, 2019
SUBJECT/REPORT NO:	Reserve / Revenue Funds and Trust Accounts Statement of Investment Policies and Procedures Review (FCS19074) (City Wide)
WARD(S) AFFECTED:	City Wide
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SUBMITTED BY:	Mike Zegarac General Manager, Finance and Corporate Services Corporate Services Department
SIGNATURE:	

RECOMMENDATION

That Appendix "A" attached to Report FCS19074 respecting the Reserve / Revenue Funds and Trust Accounts Statement of Investment Policies and Procedures dated December 5, 2019 be approved and replace the previous Reserve / Revenue Funds and Trust Accounts Statement of Investment Policies and Procedures contained in Report FCS15055 and approved by Council on September 23, 2015.

EXECUTIVE SUMMARY

Report FCS19074 requests that Council adopt the Reserve / Revenue Funds and Trust Accounts Statement of Investment Policies and Procedures (the "SIPP") dated December 5, 2019. The SIPP contains amendments arising from a formal review undertaken and required under the SIPP. The amended SIPP is attached as Appendix "A" to Report FCS19074.

The SIPP provides the framework for the investment of the assets of the City of Hamilton's Reserve / Revenue Funds and Trust Accounts. The Funds are invested in accordance with Section 418 of the *Municipal Act, 2001* and Part I of Ontario Regulation 438/97 (the "Prescribed List") and the Trusts in accordance with the *Trustee Act* (Ontario). The Historical Background section of Report FCS19074 contains comments relating to the *Municipal Act, 2001* and Part II of Ontario Regulation 438/97, Prudent Investment.

The review focused primarily on identifying any changes that impact the SIPP owing to legislative amendments in 2018 to the Prescribed List since the preceding review in 2015. There have been no amendments to *Trustee Act*, Ontario since 2015.

Several changes, listed below, are proposed for the SIPP and have been incorporated into the amended SIPP. The changes impact the investment of the Reserve / Revenue Funds, although one change (#5 below) also applies to the Trust Accounts. Changes #1, #2, #3, #5 and #6 derive from amendments made to the Prescribed List. The changes can be characterized as follows:

1. To reduce the minimum credit ratings from AA(low) to A(low) for investments in certain securities of Canadian banks;
2. To reduce the minimum credit ratings from A to A(low) for investments in Canadian corporate debt securities with a term greater than one year and less than or equal to five years;
3. To permit investments in certain securities of Canadian Schedule I banks denominated in U.S. currency;
4. To increase the maximum portfolio limit from 10% to 15% for total investments in the One Investment Program;
5. To amend the provisions that the City shall follow when an investment made in a permitted security falls below the Minimum Quality Requirements as defined in the SIPP;
6. To permit any security if the City acquires the security as a gift in a will or as a donation not made for a charitable purpose; and to require certain provisions that the City shall follow if the City acquires such a security; and
7. To revise other minor items of a housekeeping nature.

Alternatives for Consideration – Not Applicable

FINANCIAL – STAFFING – LEGAL IMPLICATIONS

Financial: Not Applicable.

Staffing: Not Applicable.

Legal: Not Applicable.

HISTORICAL BACKGROUND

According to Section 1.10 of the SIPP, the City Treasurer and Council must formally review the SIPP at a minimum once in every four calendar years.

The preceding formal review of the SIPP undertaken in 2015 is detailed in Report FCS15055 respecting Reserve / Revenue Funds and Trust Accounts Statement of Investment Policies and Procedures Review, which was approved by Council at its meeting held on September 23, 2015.

The scope of this review focused primarily on updating the SIPP to incorporate any changes in legislation impacting the SIPP since the preceding review in 2015. The proposed changes #1 and #2, as outlined in the Executive Summary of the SIPP report, would result in no alterations to the maximum limits that are imposed on these investments and set out in Appendix “A”, Sector and Issuer Limitations, of the amended SIPP. These maximum limits are seen to be appropriate at this time but might be re-considered in a future review, if deemed necessary.

Although not the subject of Report FCS19074, in 2018, legislation was introduced that would now enable eligible Ontario municipalities (other than the City of Toronto) to invest under either the Prescribed List or Section 418.1 (Prudent Investment) of the *Municipal Act, 2001* and Part II of Ontario Regulation 438/97. The latter option is often referred to as the Prudent Investor Standard.

Investing under the prudent investor standard would provide municipalities with a framework and opportunity to invest in a much wider selection of securities and investments, but before being able to invest under the standard, a municipality must adopt the prescribed governance framework.

Report FCS17097, respecting Prudent Investor Standard and Proposed Amendments to Investment and Financing Rules, included remarks that the City was part of a working group that was proposing alternative governance structures believed to better suit the investment needs of individual municipalities.

Over the last two years, the City has continued to work jointly with the Region of York, the City of Ottawa, the Region of Peel and the Region of Durham, to assess the prudent investor standard and to explore further whether alternative governance models might be permitted. Staff plan to submit a report to City Council with their findings.

POLICY IMPLICATIONS AND LEGISLATED REQUIREMENTS

The amended SIPP provides the framework for the investment of the Reserve / Revenue Funds in accordance with the Prescribed List and for the investment of monies for the Trust Accounts in accordance with the *Trustee Act* (Ontario).

Under the Prescribed List, City Council is required to adopt a statement of the City's investment policies and goals before the City invests in an investment prescribed under the Prescribed List. The SIPP is the City's statement of its investment policies and goals.

There have been no changes to the *Trustee Act* (Ontario) since the preceding review of the SIPP in 2015.

RELEVANT CONSULTATION

Staff consulted with Legal and Risk Management Services Division in the preparation of Report FCS19074.

Aon, the City's investment Consultant, reviewed the SIPP from a compliance and governance perspective. All applicable regulatory guidance was considered, and any relevant changes were addressed in the SIPP where appropriate.

ANALYSIS AND RATIONALE FOR RECOMMENDATION

The proposed changes to the City's investment policy are consistent with the objectives of the SIPP, as set out in Sections 3.02 and 5.02, conforming to legislative constraints, preserving capital, maintaining adequate liquidity and maximizing returns.

The following list contains a description of each proposed change, a rationale for the change and the section or sections of the amended SIPP reflecting the proposed change.

List of Proposed Changes

1. Minimum Credit Rating – Banks

It is proposed that the minimum credit rating be reduced from AA(low) to A(low) for investments in:

- securities of deposit receipts, deposit notes, certificates of deposit or investment, acceptances or similar instruments (“deposit securities”) issued, guaranteed or endorsed by a bank listed in Schedule I, II or III to the *Bank Act* (Canada) (“Schedule I, II or III bank”) and with a term-to-maturity of more than two years; and
- securities of bonds, debentures, promissory notes or other evidence of indebtedness (“bond securities”) issued or guaranteed by a Schedule I, II or III bank and with a term-to-maturity of more than two years.

This change is proposed because it incorporates the corresponding change made to the Prescribed List, expands investment options and allows greater flexibility.

When the term-to-maturity is less than or equal to two years, there are no changes to the requirements under the SIPP: investments in deposit securities issued, guaranteed or endorsed by a Schedule I, II or III bank must meet a minimum credit rating of A(low); and investments in bond securities issued or guaranteed by a Schedule I, II or III bank must meet a minimum credit rating of AA(low).

Appendix “A”, Sector and Issuer Limitations, of the SIPP has been amended to provide the following:

- (i) investments are permitted in deposit securities of Schedule I, II or III banks rated A(low) or higher for all term-to-maturities; and in bond securities of Schedule I, II or III banks rated A(low) or higher with a term-to-maturity greater than two years.
- (ii) A new footnote has been added that reads:

⁵ For securities of bonds, debentures, promissory notes, or other evidence of indebtedness issued or guaranteed by a bank listed in Schedule I, II or III to the *Bank Act* (Canada) with a term-to-maturity less than or equal to 2 years on the day the investment is made, the prescribed minimum credit rating is AA(low).

2. Minimum Credit Rating – Canadian Corporate Debt Securities

A change is proposed to reduce the minimum credit rating from A to A(low) for investments in bond securities issued by a corporation that is incorporated under the laws of Canada or a province of Canada and with a term-to-maturity greater than one year and less than or equal to five years.

This change is proposed because it incorporates the corresponding change made to the Prescribed List, expands investment options and allows greater flexibility. These bond securities with a credit rating of A(low) would continue to qualify as investment-grade securities (known as debt obligations which are rated BBB or higher) within the investment universe.

The following sections of the SIPP have been amended to provide the following:

- (i) The table in Section 4.06 Maximum Quantity Restrictions contains a minimum credit rating for Corporate Debt of A(low).
- (ii) Appendix “A”, Sector and Issuer Limitations, contains a minimum credit rating for Corporate Debt of A(low).

3. New Investments – Denominated in U.S. Currency

It is proposed that investments in the following securities be permitted: deposit securities in U.S. currency, for any term-to-maturity, issued, guaranteed or endorsed by a Schedule I bank with a maximum portfolio limit of 2% and with a minimum credit rating of A(low).

The City holds some U.S. currency in its bank account earmarked to pay certain obligations denominated in U.S. currency. One of the benefits to adopting this proposed change is that the City would be able to invest, if deemed advantageous, in interest bearing securities denominated in U.S. currency instead of holding the U.S. currency in its bank account until the monies are required.

This change is proposed because it incorporates the corresponding change made to the Prescribed List, expands investment options and allows greater flexibility. In the proposed change, the issuers are Schedule I banks even though the corresponding change in the Prescribed List allows not only Schedule I banks but also other eligible issuers such as Schedule II and Schedule III banks.

However, recognizing that these new investments would contain not only issuer credit risk but also potentially negative effects due to fluctuations in U.S. currency, staff recommends a conservative approach that restricts the issuers to Schedule I banks (preferred over Schedule II banks and Schedule III banks in terms of overall creditworthiness) and limits the maximum amount of investment to 2% of the total portfolio.

Schedule I banks, which include Canada's six largest banks designated by the Office of the Superintendent of Financial Institutions as domestic systemically important banks, are domestic banks whereas Schedule II banks are subsidiaries of foreign banks and Schedule III banks are foreign bank branches of foreign institutions.

The following sections of the SIPP have been amended to provide the following:

- (i) Executive Summary - Section 4: Reserve Revenue Funds - Permitted Investments has been amended to provide a revised sentence as follows:

The City shall not invest in a security that is expressed or payable in any currency other than Canadian dollars with the exception of those investments specified in Section 4.07 and footnote 6 of Appendix "A".

- (ii) Section 4.07 Currency has been amended to provide a revised sentence as follows:

The City shall not invest in a security that is expressed or payable in any currency other than Canadian dollars with the exception of those investments specified in footnote 6 of Appendix "A": investments in securities that are deposit receipts, deposit notes, certificates of deposit or investment, acceptances or similar instruments issued, guaranteed or endorsed by a bank listed in Schedule I to the *Bank Act* (Canada), expressed or payable in the currency of the United States of America, are permitted. A maximum portfolio and individual limit of 2%, within the maximum portfolio and individual limits for Schedule I banks as indicated in the Appendix "A" applies. These investments will also adhere to a minimum credit rating and a minimum money market rating requirement of A(low) and R1(low) respectively.

(iii) Appendix “A” Sector Issuer Limitations has been amended to provide a new footnote as follows:

⁶ Investments in securities that are deposit receipts, deposit notes, certificates of deposit or investment, acceptances or similar instruments issued, guaranteed or endorsed by a bank listed in Schedule I to the *Bank Act* (Canada), expressed or payable in the currency of the United States of America, are permitted. A maximum portfolio and individual limit of 2%, within the maximum portfolio and individual limits for Schedule I banks as indicated in the table above, applies. These investments will also adhere to a minimum credit rating and a minimum money market rating requirement of A(low) and R1(low), respectively.

4. One Investment Program

An increase to the maximum portfolio limit from 10% to 15% is proposed for total investments in the One Investment Program. This increase would provide the City greater flexibility to increase if deemed appropriate its investment in the One Investment Program.

The One Investment Program which is run jointly by CHUMS Financing Corporation (a subsidiary of the Municipal Finance Officers Association of Ontario) and Local Authority Services (founded by the Association of Municipalities of Ontario) offers five portfolios of investment: High Interest Savings Account, Money Market Portfolio, Bond Portfolio, Universe Corporate Bond Portfolio, and Equity Portfolio.

The Prescribed List continues to require that a municipality shall not make investments in shares or bond securities (that have a term-to-maturity greater than five years) issued by corporations that are incorporated under the laws of Canada or a province of Canada unless the municipality makes these investments through the One Investment Program. The Equity Portfolio and the Universe Corporate Bond Portfolio offer exposure to investments in these shares and to investments in these bond securities, respectively.

The following sections of the SIPP have been amended to provide the following:

- (i) The table in Section 4.06 Maximum Quantity Restrictions amended to provide a maximum portfolio limit of 15% for One Investment Program in aggregate;
- (ii) Appendix “A”, Sector Issuer Limitations, amended to provide a maximum portfolio limit of 15% for the One Investment Program.

5. Investments that Fall Below the Minimum Quality Requirements

The following change is proposed: If an investment made under the SIPP falls below the Minimum Quality Standards as defined in the SIPP, the City shall create a plan, including expected timelines, for selling the investment and shall sell the investment in accordance with the plan.

This change is proposed because it reflects the corresponding changes made to the Prescribed List. Prior to the amendments to the Prescribed List, if an investment fell below the Minimum Quality Requirements as defined in the SIPP, then the investment was to be sold within 180 days after the day the investment fell below the Minimum Quality Requirements.

Section 1.05 Downgrades in Credit Quality of the SIPP has been amended to provide the following: if an investment falls below the standard required, the City shall create a plan, including expected timelines, for selling the investment and shall sell the investment in accordance with the plan.

6. Securities Acquired as Gift or Donation

The following change is proposed: Any security is permitted if the City acquires the security as a gift in a will or as a donation not made for a charitable purpose; if the City acquires such a security that is not otherwise permitted under the Prescribed List, the City shall create a plan, including expected timelines, for selling the investment and shall sell the investment in accordance with the plan.

This change is proposed because it reflects the corresponding changes made to the Prescribed List. Previously, only certain securities acquired as a gift in a will (and the gift was not made for a charitable purpose) were permitted and were required to be sold within 90 days.

The following sections of the SIPP have been amended to provide the following:

- (i) Appendix “A”, Sector and Issuer Limitations, has been amended to provide a revised sector as follows: Security – gift in a will; or non-charitable donation:
- (ii) Appendix “A”, Sector Issuer Limitations, has been amended to provide a new footnote as follows:

¹³ Any security if the City acquires the security as a gift in a will or as a donation not made for a charitable purpose. If the City acquires such a security that is not otherwise prescribed under Part 1 of O. Reg. 438/97, the City shall create a plan, including expected timelines, for selling the investment and shall sell the investment in accordance with the plan.

7. Housekeeping Changes

The following sections of the SIPP have been amended to provide for minor changes that either enhance clarity, make corrections, or update references and nomenclature.

- (i) Section 1.11 City Treasurer's Report for the Reserve / Revenue Funds has been modified and contains:
 - A revised title that reads as follows: City Treasurer's Report for the Reserve / Revenue Funds;
 - New wording added to the first sentence as follows: "complies with Section 8 (Investment Report) of Ontario Regulation 438/97, Eligible Investments, Related Financial Agreements and Prudent Investment, under the *Municipal Act, 2001* S.O. 2001, c.25 (the "*Municipal Act*") and shall contain, but not be limited to, the following information:".
 - A new sentence that reads as follows: g) a statement by the Treasurer as to whether or not, in his or her opinion, all investments are consistent with this SIPP adopted by the City;
 - A revised sentence to read as follows: f) a statement by the CIO as to whether or not, in his or her opinion, all investments are consistent with this Statement of Investment Policies and Procedures (SIPP) adopted by the City; and.
- (ii) Appendix "A", Sector and Issuer Limitations, and Section 4.06 Maximum Quantity Restrictions: The One Funds was revised to the One Investment Program; and OSIFA was revised to the Ontario Infrastructure and Lands Corporation;
- (iii) Appendix "A", Sector and Issuer Limitations, contains the following amended footnotes:

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- ¹ Exposure percentage limitations to be applied to the par value of the total portfolio exclusive of the exposure to similar assets and/or securities held under the investments made in the One Investment Program.
 - ⁴ Prescribed securities are: deposit receipts, deposit notes, certificates of deposit or investment, acceptances or similar instruments issued, guaranteed or endorsed by a bank listed in Schedule I, II or III to the *Bank Act* (Canada); and bonds, debentures, promissory notes or other evidence of indebtedness issued or guaranteed by a bank listed in Schedule I, II or III to the *Bank Act* (Canada).
- (iv) Appendix “A”, Sector and Issuer Limitations, contains new footnotes as follows:
- ¹⁰ Minimum credit rating must satisfy R1(mid) by Dominion Bond Rating Service Limited, F1+ by Fitch Ratings, Prime-1 by Moody’s Investors Services Inc. or A-1+ by Standard and Poor’s.
 - ¹¹ One Investment Program is jointly run by CHUMS (a subsidiary of the Municipal Finance Officers’ Association of Ontario) and Local Authority Services (a corporation of the Association of Municipalities of Ontario).
 - ¹² Bonds, debentures, promissory notes or other evidence of indebtedness issued by a corporation that is incorporated under the laws of Canada or a province of Canada.
- (v) Appendix “D” of the SIPP – CFA Institute Code of Ethics and Standards of Professional Conduct reflects the most recent version from the CFA Institute.
- (vi) FTSE TMX was struck out and substituted by FTSE and Eligible Investments and Related Financial Agreements was struck out and substituted by Eligible Investments, Related Financial Agreements and Prudent Investment.

ALTERNATIVES FOR CONSIDERATION

Not Applicable.

ALIGNMENT TO THE 2016 – 2025 STRATEGIC PLAN

Our People and Performance

Hamiltonians have a high level of trust and confidence in their City government.

APPENDICES AND SCHEDULES ATTACHED

Appendix “A” to Report FCS19074 - Reserve / Revenue Funds and Trust Accounts
Statement of Investment Policies and Procedures dated December 5, 2019.

RM/dt