

TO: CHAIR AND MEMBERS
FINANCIAL MANAGEMENT COMMITTEE

DATE: 2020 March 02

FROM: DIRECTOR FINANCE

FILE: 7500-01

SUBJECT: EXPANDING INVESTMENT OPPORTUNITIES

PURPOSE: To provide an update on the prudent investor rules UBCM resolution.

RECOMMENDATION:

1. **THAT** the Financial Management Committee receive this report for information.

REPORT

1.0 INTRODUCTION

On 2019 April 24, the Financial Management Committee presented a report to Council, seeking support for the submission of a Union of Municipalities British Columbia (UBCM) resolution requesting the Ministry to review section 183 of the *Community Charter* for the purpose of making changes to the current prescribed methodology for municipal investments. The goal being the expansion of asset class investments through prudent investment standards as a means of reducing portfolio risks while ensuring long term municipal financial sustainability.

With Council approval, the City of Burnaby submitted the resolution which was identified as B128 (2019) and reads as follows:

B128 Expanded Asset Class Investments Under Prudent Investor Rules

- *Whereas financial investments form a critical part of the activities of a municipality, providing a source of revenues for capital expenditures and to offset cash flow fluctuations;*
- *And whereas allowable investment parameters as laid out in the Community Charter is considered a "prescribed" set of legislated guidelines;*
- *And whereas the Provinces of Alberta and Ontario have implemented a wider scope for local government investment, which responds to the needs of local governments of all sizes;*
- *Therefore be it resolved that UBCM request the Ministry of Municipal Affairs and Housing to amend the Community Charter to provide municipalities with the ability to obtain improved returns through asset class diversification, which in return can reduce tax implications and funding costs associated with capital funding, while also reducing investment risk.*

The Ministry of Municipal Affairs and Housing has now responded to all presented resolutions from the annual September 2019 Convention. Specifically, this report provides information about the response from the Ministry regarding item B128 (2019) and information on the next steps the City of Burnaby and Municipal Finance Authority intend on taking to further investment risk reduction through asset class diversification, improved long term yields and income generation via an MFA sponsored Growth Pooled Fund.

2.0 POLICY SECTION

Goal

- A Connected Community
 - Partnership –
Work collaboratively with businesses, educational institutions, associations, other communities and governments
- A Dynamic Community
 - Economic opportunity –
Foster an environment that attracts new and supports existing jobs, businesses and industries
 - Community development –
Manage change by balancing economic development with environmental protection and maintaining a sense of belonging
- A Thriving Organization
 - Financial viability –
Maintain a financially sustainable City for the provision, renewal and enhancement of City services, facilities and assets

3.0 PRUDENT INVESTMENT STANDARDS

3.1 Ministry of Municipal Affairs and Housing Response

The Ministry of Municipal Affairs and Housing has recently responded to UBCM resolutions through the convention website. Dated February 2020, the Ministry has provided the following written response for resolution B128 (2019):

- *Local governments are responsible for public money (from taxpayers, developers, and others) for provision of core services and upkeep of critical infrastructure. As such, preservation and protection of financial capital is the foremost objective of provincial legislation governing local government investments. Accordingly, the current legislation limits investment risk and guides local governments toward high-quality, secure investments that will contribute to the fundamental goal of capital preservation while allowing a reasonable rate of return.*

- *Under the current provisions, all local governments, regardless of size and capacity, have access to a prescribed list of allowable investments including the Municipal Finance Authority's (MFA's) pooled investment funds.*
- *As the Province's primary objective regarding local government investments is to ensure protection of capital through low-risk instruments, the Ministry is not currently prepared to expand the allowable investment provisions.*

The Ministry has determined that providing prudent investment standards to individual municipalities, similar to the changes made in Ontario and Alberta, is not warranted. While not the response the supporting municipalities of the resolution were looking for, the benefits of asset class diversification, which improves risk diversification, long term sustainability and long-term capital preservation, remains a goal. Therefore, City staff have already begun discussing alternatives with the MFA, which as noted by the Ministry in their response, can offer pooled fund investment options for municipal investment needs.

3.2 Municipal Finance Authority – Investment Pooled Funds

Part 6, Division 3, Section 183 of the *Community Charter* provides the prescribed list of permitted investments for British Columbia municipalities. These legislated guidelines state that municipalities may invest or reinvest money that is not immediately required into several distinct categories of fixed income investments (bonds, money market instruments, or deposits issued by municipalities, federal or provincial governments, banks, saving institutions or credit unions).

In addition to those categories, the first two parts of the *Community Charter* Section 183, provides for municipal investment opportunities specifically in MFA securities or pooled funds. The section reads as follows:

183 Money held by a municipality that is not immediately required may only be invested or reinvested 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*;

The City of Burnaby can invest in securities issued by the MFA and in 2020 we began investing in the MFA Pooled Mortgage Fund which provides important asset class diversification for the portfolio. The City also awaits the creation of the MFA Fossil Fuel Free Bond Fund, pending MFA Board of Trustees approval in March, for which the City has committed to invest up to \$20 million.

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The MFA has recognized the importance of working with municipalities in providing investment products and investment education while leveraging the expertise of various municipal staff across the Province. In 2019, the MFA created a Pooled Fund Advisory Committee (PFAC) to assist MFA staff in creating and managing pooled funds. The City of Burnaby's Assistant Director Treasury Services is a PFAC committee member. The MFA plays a very important role in assisting municipalities with investment diversification options via pooled funds and consults with municipal partners to review the structure and performance of the pooled funds, including holding roundtable discussions to ensure future municipal needs are discussed and analysed. It is in these arenas that prudent standards and growth focused investments have garnered attention, especially since Ontario made headlines in 2018 and 2019 with the introduction of their own prudent investor regime for all municipalities.

It appears that the MFA Act (together with the Trustee Act) already provides the platform needed to meet the needs of municipalities wanting to adopt prudent standards and introduce higher return/longer term assets into reserve portfolios. The MFA Act provides under section 16 (e) the authorization for the MFA to create pooled funds utilizing "investments permitted under the provision of the Trustee Act". The Trustee Act provides for the investment of funds by a trustee in a manner that a prudent investor would exercise in making investment decisions. The MFA Act therefore provides for prudent investment standards to be applied to pooled funds created by the MFA for municipal investments without any limitation as to asset type, including equities or other alternative investments.

The City of Burnaby has been working with the MFA staff for about one year now, meeting jointly with various asset managers and consultants, to analyse the best approaches to achieving asset class diversification for long term growth investments that are not required for 10 years or even longer. The partnership we have established was made in order to leverage both Burnaby's and MFA's investment expertise with a view that, regardless of the Ministries response, Burnaby's Treasury Staff supported by the Council's resolution, was likely to recommend moving forward with the introduction of higher return investment options for a portion of its own reserves. We understand that MFA staff has had preliminary discussions with its own Board of Trustees on this topic. We also understand that, at the next Annual General Meeting in March 2020, the MFA Chief Executive Officer, Peter Urbanc will provide its Members with an update on the Minister's response to B128 (2019) and discuss the next steps that MFA staff would need to undertake to add a growth pooled fund to its pooled fund offerings.

Likely steps would include obtaining legal opinion(s), continued analysis of the type of fund to be created (what assets to be included), continued discussions and reporting to the Board of Trustees, needs analysis by municipalities (including how to segregate reserves as long term in nature), discussion(s) with the Inspector of Municipalities and other Ministries. These steps are aimed at providing full transparency and enable the MFA and Burnaby to appropriately identify and educate the entire local government sector of benefits and mitigate risks involved. A critical part of this process is educating those many local governments who have limited financial staffing resources on the risks and limitations associated with long term growth investments if they are not segregated as such. Not only must robust long term asset management and cash flow processes be in place to identify

long term reserves, but a mechanism to ensure that a local government that plans for the long term and decides to buy a growth oriented pooled fund remains disciplined and does not decide to change its mind mid-stream (for example, right after a market correction).

The partnership between the MFA and the City of Burnaby has created many benefits over the last few years as we share information, provide educational sessions to other municipalities and plan for future needs to ensure long term sustainability for capital needs. Many municipalities are now joining the discussions and seeking longer-term fund growth opportunities and improved portfolio diversification to mitigate the various risks based on current practices and legislated limitations.

3.3 City of Burnaby – Portfolio diversification and long term reserves

The UBCM resolution submission was a means to getting the conversation started through an official response from the Ministry of Municipal Affairs and Housing. Staff's rationale for the request has not diminished. In fact, strong support for the resolution, ongoing communications from other municipalities, and our joint work with the MFA and asset managers has clarified that a change is desired and prudent. Many municipalities, whose reserves often exceed their short-term needs, are seeing the value of their investments eroding as an ultra-low interest rate environment provides investment returns that are most often below the general rate of inflation, and certainly below the inflation on capital asset maintenance or replacement.

Investing a portion of Burnaby's reserves into a diversified portfolio of global equities, fixed income and other investments would build a stronger more balanced, sustainable reserve portfolio by decreasing asset type and credit concentration risks while increasing long term expected returns. We recognize that the taxpayer cannot (and should not) be the sole bearer of the fast-rising costs of capital infrastructure and our current suboptimal investment parameters certainly impact future taxation negatively. A move to expanded asset classes is not solely a reaction to historically low money market and fixed income interest rates. Such a move is also a risk mitigation measure which allows a broader allocation of investments across many financial categories, industries and instruments. It aims to maximize returns by matching long term investments with long term needs that are growing at faster than the general inflation rate. Under the current prescribed methodology, this prudent approach is simply not possible.

For the City of Burnaby, should an MFA long term growth fund come to fruition, staff would be recommending a maximum allocation of \$340 million, which represents approximately 20% of the City's current portfolio. While not an overly aggressive amount, this represents funds not required immediately and can be invested long term, such as funds held within the Corporate & Tax Sale Land Reserves, Equipment Replacement Reserves, Unallocated DCC Reserves and Water and Sewer Capital Reserves.

4.0 SUMMARY

Over the last ten months, a great deal of discussions have occurred around prudent investment standards, long term sustainable reserve growth and risk mitigation obtained through asset class diversification. The City of Burnaby submitted a UBCM resolution requesting a change to the Community Charter section 183 and the Ministry has now responded to that September 2019 submission stating that they will not make a change to the current legislation. The Ministry however confirmed the role of the MFA in supporting municipal investment needs, making an implicit statement about BC local governments' access to MFA's pooled investment funds.

City of Burnaby staff and the MFA continue to work together on analyzing the opportunity of providing a growth fund solution to qualifying municipalities. This analysis and effort is garnering momentum as supporting municipalities are looking at alternative strategies and opportunities. Many are recognizing that the current investment landscape and prescribed investing legislation is introducing risks into the system. The activities of the MFA, through the creation of new pooled funds and high interest savings accounts over the last 18 months, have been strongly supported by municipalities across the province. The MFA and the City of Burnaby, through leadership and knowledge transfer, has been increasing municipality awareness of the market and fiduciary responsibilities when making investment decisions.

City of Burnaby staff will continue working with the MFA as they can now move forward on deeper discussions with their Board of Trustees around prudent investment standards and how those may be used to create a new class of multi-asset growth pooled fund(s) in the future. We intend on participating actively in that dialog and recognize that a thoughtful process, including dialog with other local governments, asset managers, lawyers, and Provincial Ministries will take place as a means of clarifying the benefits and mitigating the risks involved, while providing transparency

As this effort evolves and information is made available, staff will provide updates to Council prior to making any official recommendations for equity or other growth asset investment product participation.



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