



Date: 31/05/2019

AGENDA ITEM SUMMARY

To: Chair and Directors, Cariboo Regional District Board

And To: John Maclean, Chief Administrative Officer

From: Kevin Erickson, Chief Financial Officer

Date of Meeting: Cariboo Regional District Board_Jun27_2019

File: 400-50-01

Short Summary:

Request for Support from City of Burnaby for UBCM Resolution on Expanding Investment Opportunities for Local Governments

Voting:

Corporate Vote - Unweighted

Memorandum:

The City of Burnaby intends to put forward a motion to the Union of British Columbia Municipalities to request the Ministry of Finance to amend the *Community Charter* to allow Local Governments more latitude in investing opportunities.

Attachments:

- 1) Letter from the City of Burnaby dated May 02, 2019
- 2) Report to the City of Burnaby Financial Management Committee on Expanding Investment Opportunities, April 17, 2019

Financial Implications:

The City of Burnaby is seeking support for a change to the *Community Charter* that would broaden the scope of products local government could invest funds in to earn better returns. Towards this they put forward the concept of adopting “Prudent Investor Rules” as a replacement to the prescribed investments of the *Community Charter* and provide information on how this has been applied in other jurisdictions. Currently, local government investing opportunities are restricted through Section 183 of the *Community Charter*:

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;
- c) Securities of Canada or 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, non-equity or membership shares of a credit union;
- h) Other investments specifically authorized under this or another Act.

As Burnaby points out these investments are prescribed. As such they are not the highest earning instruments, but they are as safe as any investment can be.

The City of Burnaby's proposal is to replace these prescriptions of Section 183 with a Prudent Investor Rule requiring "the investment manager of an organization to conduct investment activities with care, skill and due-diligence for that which a prudent person would do when managing their own investments..." This would allow local governments to seek other investment opportunities such as real estate and equities. What is being asked is to change the way local governments invest their free cash. Moving to a Prudent Investor Standard would change investing to an active endeavor where maximizing returns becomes the objective.

Recognizing that there is great disparity among municipalities with regards to resources, both people and monetary, Burnaby puts forward that any governance "must consider inclusion for all without creating additional costs and risks." "Such risks can be mitigated through pooling investments or contracts with qualified funds managers through the set-up of simplified but effective reporting standards and clear guidelines." Effectively, smaller local governments like the CRD would have to outsource the management of their investments to a fund manager while large local governments, with sufficient resources, could internalize their management by hiring staff with the necessary knowledge and skills of portfolio management. The reports position is that the returns after management fees will be better than the returns that can be earned passively and justifies the additional risk inherent in these types of investments.

The report, while acknowledging there are certain risks in moving to an active investment strategy tends to focus on the positive aspects and not address mitigation of these risks. Reporting standards and clear guidelines are no assurance if someone is purposefully working around them. They do not acknowledge that, in chasing returns an investment manager may not stay within defined parameters of the local government's risk preferences. Similarly, the definition of a prudent person and how they manage their own investments is subject to the risk tolerance of the individual. This raises the possibility that the risk tolerance of the person or persons managing the local government's investments may not align with the local government or its taxpayers. Equities are variable in nature. As the report notes, a "longer term investment time horizon ... is needed under other asset classes such as equities and real estate." Increased volatility means an increase in the reporting of gains and losses from price swings. Similarly, an investment that is long-term in nature takes away the liquidity of the investment and thus restricts the local governments access to the funds. An underperforming investment in equities or real estate could convince the local government to take on more debt in hopes the investment turns around rather than recognize the loss by cashing out. Conversely, because the returns are so good at the time funds are needed more debt might be taken on because the borrowing rate is less than the rate of return on investment. In both instances, active investing has now subverted the reason for having collected the funds in the first place.

The report also downplays the possibility of a local government getting into a worst-case scenario where, through bad decisions or lack of oversight, they suffer a total loss which materially impacts the financial capacity of the local government. A possibility when investing

activities are motivated to maximize returns. It is easy to say it can't happen but, if it does, what mechanisms do they foresee being in place to deal with it.

Changing to a Prudent Investor Rule is an issue worth exploring further, especially because of the opportunity to earn higher returns and provide tax relief for citizens. The City of Burnaby's committee report does a good job of pointing out the potential benefits of expanded investment opportunities. The objective is not to rebut Burnaby Council's request for support, only to raise awareness that higher returns are a result of higher risk and that market failures can and do occur.

Policy Implications:

n/a

Alignment with Strategic Plan:

- ☒ Ensuring Sufficient and Sustainable Funding
- ☐ Building on our Relationships
- ☐ Providing Cost Effective High Quality Services
- ☐ Focusing on Being Well Governed

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CAO Comments:

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Options:

- 1) Receipt
- 2) Receipt and other action

Recommendation:

That the agenda item summary from Kevin Erickson, Chief Financial Officer, dated May 31, 2019, regarding a request from the City of Burnaby to support a UBCM resolution on expanding investment opportunities for local governments, be received. *Further action at the discretion of the Board.*