

## **Establishment of an Investment Board**

**Date:** February 21, 2017

**To:** Executive Committee

**From:** City Manager and Deputy City Manager & Chief Financial Officer

**Wards:** All

### **SUMMARY**

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This report recommends that City Council establish an Investment Board (the Board) to manage and invest City funds which are not immediately required, pursuant to Regulation 610/06, Financial Activities, of the City of Toronto Act, 2006. This Regulation comes into force on January 1, 2018 and introduces much greater flexibility with the City's investment powers but prescribes that City Council must exercise this expanded authority through a City Investment Board.

The Board is required to exercise its investment authorities pursuant to the prudent investor standard and in compliance with an Investment Policy approved by City Council. The prudent investor standard sets parameters for those entrusted with the responsibility of managing others' money, and requires that they weigh risk versus reward when making investment decisions, taking into account the income that may be generated by the investment as well as the probable safety of the invested capital.

This report recommends the governance structure for the Investment Board including mandate and responsibilities, composition and eligibility, qualifications of members and Chair, remuneration, term and appointment process and accountability and reporting.

Lastly, the dissolution of the Independent Investment Advisory Committee, established in April 2011 to advise the Deputy City Manager & Chief Financial Officer on portfolio strategies and governance issues for the City's investment portfolios, is recommended as the Investment Board will now have responsibility for managing and investing the City's portfolios.

### **RECOMMENDATIONS**

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The City Manager and Deputy City Manager & Chief Financial Officer recommend that:

1. City Council establish an Investment Board and delegate its authority to the Board to manage and oversee the City's investments of funds not immediately required by the

City, as is required by Regulation 610/06, Financial Activities, under the City of Toronto Act, 2006 and pursuant to the governance structure outlined in Attachment 1 of this report.

2. City Council direct that a separate Toronto Municipal Code Chapter be established for the Investment Board substantially as provided for in Attachment 1 to this report and authorize the City Solicitor to bring forward the necessary bills.

3. City Council authorize the City Clerk to initiate a recruitment process for Investment Board members for review by the Facilities and Finance Nominating Panel for recommendation of appointment by City Council.

4. City Council direct the City Clerk to provide secretariat support to the Investment Board.

5. City Council direct the Deputy City Manager & Chief Financial Officer to support the implementation and ongoing maintenance of the Investment Board.

6. City Council approve an interim 2017 budget of \$557,500 for the Investment Board as detailed in Attachment 2 and funded from non-program investment income.

7. City Council request the Integrity Commissioner to review the Code of Conduct for Local Boards and recommend any required amendments to the Code of Conduct for the Investment Board given its fiduciary responsibilities.

8. City Council dissolve the Independent Investment Advisory Committee effective December 31, 2017.

## **Implementation Points**

Implementation of the establishment of an Investment Board will commence upon City Council's approval of this report. Key activities to implement the Investment Board are summarized below and must be completed prior to its first meeting.

It is anticipated that the Investment Board will be in place by summer 2017 to begin preparatory work in advance of the Regulation coming into force on January 1, 2018.

### *Recruitment and Appointment Process*

The City Clerk's Office will begin the process to recruit members. The Facilities and Finance Nominating Panel will screen, interview and recommend candidates for appointment by City Council including a Chair. It is anticipated that Investment Board members will be appointed by summer 2017.

As per the Ontario Regulation, City Councillors and City staff, with the exception of the statutory City Treasurer, are prohibited from being members of the Investment Board.

## *Operational Readiness*

The Deputy City Manager & Chief Financial Officer, through the Corporate Finance Division, in consultation with the City Manager and City Solicitor, will facilitate operational readiness so that the Board will be prepared to assume its mandate and responsibilities by January 1, 2018. This work includes drafting a Procedural By-law for consideration by the Board, setting the ground work for procuring external investment experts for use by the Board, and ensuring the Board has provided input on the draft Investment Policy that it will be responsible to implement. When the Board is in place, it will be responsible to develop an Investment Plan that implements the Council approved Investment Policy.

## **FINANCIAL IMPACT**

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Costs associated with the establishment and administration of the Investment Board will be funded directly through non-program investment earnings and will have a net zero budget impact.

An interim budget for the last six months of 2017 is found in Attachment 2. These initial costs include: Investment Board member remuneration; costs for developing an Investment Plan and Strategy as well as for procuring investment agents and related consulting services; and staff costs. These interim costs are estimated at \$557,500. A full budget will be developed as part of the 2018 budget process.

The Deputy City Manager & Chief Financial Officer has reviewed the report and agrees with the financial impact statement.

## **DECISION HISTORY**

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At its meeting of March 2016, City Council adopted the report, *New Investment Regulations*, which requested the Deputy City Manager and Chief Financial Officer to report back on: the overall objectives of the City's investment policy, the qualifications for members of the investment board and a plan for how the City will prepare to have the investment board in place for January 1, 2018.

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2016.EX13.10>

At its meeting on April 12 and 13, 2011, City Council, among other things, established a new Independent Advisory Committee in accordance with the City's Public Appointment Policy to advise the Deputy City Manager & Chief Financial Officer on portfolio strategies and governance issues for all of the City's investment portfolios.

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2011.EX4.6>

## **ISSUE BACKGROUND**

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Since the inception of local government in Ontario, the Municipal Act and more recently, the City of Toronto Act, 2006, prescribed the investments that were permitted to be used by municipalities. The prescribed investments, consisting mainly of fixed income securities such as debentures and bonds of various maturities and shorter-term treasury bills and chartered bank deposits, are considered to be highly restrictive and limited the type of securities that municipalities could invest in.

This investment regime worked well for a number of years, providing local governments with reasonable rates of return with minimal risk. However, given the prolonged low inflation and interest rate environment in recent years, rates of return on these funds has decreased by more than 50% from an average of 6% to under 3% in many cases. This has resulted in a significant decrease in investment earnings with consequential fiscal impacts.

The City of Toronto is a mature order of government that can decide how best to invest its financial assets. Previous legislation was overly prescriptive and restrictive and prevented the City from optimizing its risk adjusted returns. The Province, in recognition of these shortcomings, moved to change the Regulation to allow for broader investment powers under a concept known as the "prudent investor standard". This standard has been in place for a number of years in Ontario for pensions and endowments, however the City of Toronto will be the first municipality in the province to be allowed to use this standard.

The "prudent investor standard" is defined as the standard of fiduciary duty for those entrusted with the responsibility of managing others' money, such as trustees and estate administrators. It requires that a trustee weigh risk versus reward when making investment decisions, taking into account the income that may be generated by the investment as well as the probable safety of the invested capital.

## **COMMENTS**

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### **1. Establishment of an Investment Board**

The Province of Ontario approved amendments to Ontario Regulation 610/06, Financial Activities, under the City of Toronto Act 2006, to provide a framework for the City to invest according to the prudent investment standard. These amendments allow the City to add securities such as equities and non-bank corporate bonds to its current holdings.

The prudent investor standard is a well-established benchmark by which to measure investment decisions and is the standard required of trustees in Ontario under the Trustee Act. This change allows the City to invest in a much broader class of securities provided it exercises the care, skill, diligence and judgement of a prudent investor having regard for relevant economic and financial criteria and the City's appetite towards risk and its need for liquidity.

The amendments to Ontario Regulation 610/06, signifies a significant shift towards providing the City with more flexibility in making investments but also requires City Council to exercise this enhanced authority through a City Board.

This report therefore recommends that City Council establish an Investment Board under subsection 46(2) of Ontario Regulation 610/06 and delegate its authority to control and manage investments of funds not immediately required by the City to the Board pursuant to the prudent investment standard and an Investment Policy adopted by City Council. The Independent Investment Advisory Committee, established in 2011 to provide advice to the Deputy City Manager & Chief Financial Officer on portfolio strategies, will be dissolved effective December 31, 2017 as the Investment Board will now be responsible for managing the City's investments.

## **2. Investment Policy**

The Regulation requires that City Council adopt an Investment Policy that the Investment Board will be responsible to implement through an Investment Plan. The Investment Policy must consider the general economic conditions, the possible effect of inflation and deflation and the role each investment plays within the City's portfolio. The Investment Policy must also address the City's objectives for return on investment, risk tolerance and liquidity needs for planned projects and unanticipated contingencies. City Council is required to review and update its Investment Policy annually.

The Deputy City Manager & Chief Financial Officer will be submitting a separate report on an Investment Policy for consideration by Executive Committee within the next few months. The report will recommend that City Council approve the Investment Policy in principle in order that the Investment Board has an opportunity to review and provide input into the Policy prior to final approval by City Council. It is anticipated that the final Investment Policy will be submitted to Executive Committee in fall 2017.

## **3. Governance Structure of the Investment Board**

A third party consultant was retained to undertake jurisdictional research of similar public and private boards to benchmark key governance provisions related to term, composition, qualifications, and remuneration.

The recommended governance structure discussed below and summarized in Attachment 1 to this report considered the third party research as well as legal and regulatory requirements for the Investment Board. A separate Municipal Code Chapter to establish the Investment Board is also recommended.

### *A. Mandate and Authorities*

The Investment Board is a City board, established under subsection 46(2) of Ontario Regulation 610/06, responsible to control and manage the City's investments in funds not immediately required by the City pursuant to the prudent investment standard and an Investment Policy adopted by City Council.

The Board is responsible to adopt and follow an Investment Plan that implements the City's Investment Policy. The Investment Plan shall deal with how the Board will invest the City's money and set out its projections of the proportions of the City's portfolio to be invested in particular investments.

At least annually, following City Council's review of the Investment Policy, the Board is required to review its Investment Plan and update it as required. The Board may retain agents to act on their behalf pursuant to the requirements in Regulation 610/06.

#### *B. Composition and Eligibility*

The Investment Board will be composed of seven (7) members, including a Chair and one of the members will be the City's statutory Treasurer appointed under section 138 of the City of Toronto Act, 2006. Provincial regulation prohibits officers or employees of the City and Council members from appointment to the Board with the exception of the statutory Treasurer. The Regulation requires the statutory Treasurer to advise City Council if the City's investments are not compliant with the City's Investment Policy and the Board's Investment Plan.

The Deputy City Manager & Chief Financial Officer currently holds the statutory Treasurer appointment. It is City staff's view that including the Deputy City Manager & Chief Financial Officer in his capacity as statutory Treasurer on the Board will provide the necessary expertise to the Board and ensure coordination.

The Investment Board members will also be required to meet the eligibility requirements pursuant to the City's Public Appointments Policy including that they are a resident of Toronto and at least 18 years of age. Additionally, given the fiduciary responsibilities of the Board, members must not have declared bankruptcy, or had disciplinary action by a security regulator or self-regulating investment organization in the past twenty (20) years.

#### *C. Term*

The term for Investment Board members will be subject to the term requirements of the City's Public Appointments Policy which provides for terms of 4 years until successors are appointed, served at the pleasure of City Council. The maximum term pursuant to the City of Toronto Act, 2006 is two (2) four (4) year terms.

Staggered terms are recommended with three (3) members being appointed for four (4) years and three (3) members being appointed for two (2) years to ensure Board continuity.

#### *D. Qualifications of Members*

It is important that Investment Board members are experienced and skilled to help ensure high quality decision-making consistent with their fiduciary responsibilities. The qualification of members is particularly important given the amount of the portfolio they will be responsible to invest and their delegation of authority in this regard.

Public members of the Board shall collectively represent a range of skills, knowledge and experience to discharge their duties in an effective manner including:

- Executive level experience in a major public or private organization;
- Senior level experience in the investment industry such as the management of institutional portfolios including pension funds, endowments, foundations, mutual funds, and closed-end funds;
- Professional skills relating to investment and/or debt management as well as an understanding of risk and financial administration within the framework of the prudent investor standard;
- Post-graduate degree in any one of the fields of: finance, business, economics, risk management, accounting, public administration or related fields that may include certification such as CFA designation, Canadian Investment Manager Certification or equivalent;
- Possession of sound judgement and knowledge of good governance; and
- Understanding of the principles of public accountability and integrity.

A minimum of three (3) board members must have senior level experience in the investment industry such as the management of institutional portfolios including pension funds, endowments, foundations, mutual funds, and closed-end funds.

#### *E. Role and Qualifications of the Chair*

In addition to the responsibilities and duties of Board members, the Chair will be responsible to ensure meetings are effective, decisions are consistent with the Board's mandate and that the Board holds regular business meetings as required. The Chair will also prepare for approval by the Board an annual report to City Council and coordinate operational activities of the Board including liaising with the City Clerk's Office and Corporate Finance as necessary.

The Chair will need to be an effective leader and will be required to demonstrate additional expertise and skills in order to perform this role effectively including well-developed leadership and administrative skills. In addition to the qualifications of Board Members, the Chair will be required to demonstrate the following qualifications:

- Leadership and administrative skills;
- Highly developed chairing and facilitation skills; and
- The ability to effectively represent the Board and communicate with City Council, City Committees, City staff, the media and general public.

#### *F. Chair and Member Remuneration*

The recommended remuneration for the Chair of the Investment Board is an annual \$50,000 retainer and \$750 per board meeting. The recommended remuneration for Board members is an annual \$10,000 retainer and \$750 per board meeting up to a maximum of \$25,000. Board members will also be remunerated \$500 for attending business meetings of the Board estimated at two (2) business meetings per year. It is estimated that the Board will meet six (6) to eight (8) times per year.

The remuneration is intended to attract qualified applicants and compensate members for the high level of fiduciary responsibility and work involved in this board. The remuneration is generally consistent with the remuneration levels at City Corporations namely Build Toronto, Toronto Community Housing Corporation and Toronto Hydro.

#### *G. Appointment Process*

The City Clerk's Office will be responsible for recruitment and outreach and to encourage citizens to make an application for consideration of appointment to the Board. The Facilities and Finance Nominating Panel will review, short-list and interview applicants and recommend candidates for appointment by City Council.

### **4. Accountability Provisions**

The Board will be responsible to manage and invest an estimated \$5 billion portfolio on the City's behalf. Given the high level of fiduciary responsibility for the Investment Board, it is imperative that appropriate accountability mechanisms be established.

The accountability provisions for the Investment Board are summarized below.

- **Jurisdiction of the Accountability Officers** - consistent with other local boards of the City, the Investment Board will be within the jurisdiction of the Auditor General, Integrity Commissioner, Lobbyist Registrar, and Ombudsman.
- **Code of Conduct for Local Boards** - the Board is required to comply with the Code of Conduct for Local Boards.
- **Open Meeting Requirements** - consistent with other local boards, the Investment Board is also required to conduct its meetings in accordance with the open meeting requirements of the City of Toronto Act, 2006.
- **Annual Review of its Investment Plan** - the Board is required, following City Council's annual review of its Investment Policy, to review its Investment Plan and make amendments to comply with the Investment Policy as required.
- **Annual Report to City Council** - the Board is required to provide an annual report to City Council about the performance of the City's portfolio, and an assurance from the Treasurer that the investments are consistent with the City's Investment Policy adopted by City Council and as amended from time to time.
- **Annual Compliance Audit** - to assist the Treasurer with providing an assurance to City Council on an annual basis that the Board is investing in compliance with the Council adopted Investment Policy, a third party auditor will undertake an annual compliance audit on behalf of the Treasurer.



## 5. Code of Conduct Considerations

The Investment Board will be subject to the Code of Conduct for Local Boards and is within the jurisdiction of the Integrity Commissioner. The Code of Conduct for Local Boards sets out high standards for citizen appointees to City boards appointed by City Council to act on its behalf. The Code sets out requirements with respect to gifts and benefits, confidential information, use of City and board resources, election campaign work, improper use of influence and conduct guidelines related to employment, meetings, interactions with staff, and lobbyists.

The Investment Board will be managing a large portfolio of investments on behalf of the City and given these fiduciary responsibilities, the Code of Conduct for Local Boards may not be adequate. This report therefore recommends that City Council request the Integrity Commissioner to review the Code of Conduct for Local Boards within the context of the mandate and responsibilities of the Investment Board and report back with any amendments as may be required. The City already has a precedent for a Code of Conduct specific to a particular classification of local boards given there is a separate Code of Conduct for Adjudicative Bodies that considers their particular mandate and context.

### CONTACT

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### SIGNATURE

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Rob Rossini  
Deputy City Manager & Chief Financial Officer

Peter Wallace  
City Manager

### ATTACHMENTS

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Attachment 1 - Governance Structure of the Investment Board  
Attachment 2 - 2017 Interim Budget