

Investment Policy



CITY OF
MINNEAPOLIS, MINNESOTA

April 2019

FINANCE & PROPERTY SERVICES DEPARTMENT
Investments Capital and Debt Management Division

I. Introduction

It is the policy of the City of Minneapolis that the administration of its funds and the investment of those funds require the public's highest trust. The Investment Policy of the City of Minneapolis (the "City") defines the parameters within which funds are invested. The policy establishes the framework for the City's investment program to ensure effective and judicious investment of the City's funds. The Policy is intended to be broad enough to allow investment officer(s) to function properly within the parameters of responsibility and authority, flexible enough to address changing market conditions, and specific enough to safeguard investment assets. The receipt of a market rate of return will be secondary to the requirements for safety and liquidity. The earnings from investments will be used in a manner that best serves the interests of the City and its various specialized funds.

The Investment Policy will be reviewed by the City's Chief Financial Officer (CFO), at least annually and any recommended changes shall be taken to City Council for review and consideration. No changes may be made until the Policy is reviewed and adopted by the City Council.

II. Governing Authority

The Policy and investment program shall be administered in conformance with applicable federal, state, and City statutes and requirements, specifically Minnesota Statutes Chapter 118A. The City's Internal Controls and Procedures for Investments support all requirements of this Policy.

III. Scope

The Policy shall apply to the City's cash and investments regardless of source and any new funds created unless specifically exempted by the City Council and this Policy. Assets held by trustees or fiscal agents for specifically designated programs or financial arrangements may be regulated by other policies or governing City Council actions and guidelines. However, all City funds invested are subject to statutes and regulations established by the State of Minnesota.

Cash and investments specifically excluded from this Policy are employee retirement funds (held and managed by the State Board of Investment), and employee health savings accounts (held and managed by third party administrators).

IV. Portfolio Objectives and Strategy

The City commingles its cash for investment purposes. This adds value to all the funds while portfolio and general ledger reporting assures that all earnings are returned to appropriate source funds based on general ledger balances and budget practices, as appropriate. Participation in the commingled portfolio assures each participating fund safety and liquidity.

It is the policy of the City that all funds are invested with four primary objectives listed below in order of their priority.

1. Safety

Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital.

2. Liquidity

The investment portfolio shall be structured to meet operating requirements that may be reasonably anticipated. This shall be achieved by matching investment maturities with forecasted cash flow requirements and maintaining an adequate amount of cash or cash-like instruments for unexpected outflows. The portfolio should generally consist of securities with active secondary markets and readily determinable market values.

3. Diversification

The portfolio shall be diversified to eliminate the risk of loss resulting from over-concentration of assets in any specific maturity, specific issuer, or specific market sector.

4. Yield

The investment portfolio shall be designed with the objective of attaining a reasonable market yield throughout budgetary and economic cycles, considering the investment risk constraints of safety and liquidity. The portfolio yield will be measured against established benchmarks.

Local Considerations

Subject to the above portfolio objectives, the City will encourage qualified local financial institutions within the City to participate in the request for proposals (RFP) process to provide professional services and investments necessary for the administration of the investment program.

Portfolio Strategy

The City shall pursue a pro-active yet conservative portfolio management strategy. The City's total portfolio is divided into four segments/sub-portfolios to address (1) the ongoing fiscal year demands of the City's operating funds, (2) the bond proceeds which are guided by expenditure schedules of the bonds, (3) the 'core' funds which are reserved for future needs, and (4) the debt service reserves which are required reserves for the underlying bonds.

The strategy for each of these segments incorporates the specific uses and the unique characteristics of the funds in the segment/sub-portfolio. For all City portfolios the strategy is designed to safeguard principal and maximize earnings within designated risk and term parameters.

The strategy for the *operating portfolio* is to match investment maturities with the operational needs of the City throughout its fiscal year, and longer if conditions warrant. The maturities for securities in this portfolio will generally be within two years. The Operating portfolio for the City will be managed internally.

The strategy for the *bond proceeds portfolio* is to invest bond proceeds pro-actively to the anticipated expenditure schedule for the projects financed as updated from time-to-time. Because most bond proceeds are expended within a few months to three years of issuance, the maturities for securities in this portfolio will be less than three years. Portfolio managers must adhere to maturity and duration parameters established, and revised periodically.

The strategy for the *core portfolio* is to pro-actively manage the funds with a longer maturity schedule than other portfolios. The resulting longer maturities may result in unrealized losses in the City's annual financial statements. However, realized losses, are allowed if they will provide a net gain to the portfolio over a reasonable period. The dollar weighted average maturity for this portfolio will generally be within five years, although an individual security could have a maturity greater than five years. External Investment managers of core funds must adhere to maturity and duration parameters established, and revised periodically.

A portion of the core portfolio is allowed to exceed the five-year weighted average maturity, but not to exceed 10 years in total term if funds are used for one of the following purposes:

1. The Chief Finance Officer may utilize cash to prepay outstanding City bonds or notes or create internal loans in lieu of performing bond refunding transactions.
2. The City may designate up to 10% of the core portfolio(s) to be invested in securities supporting naturally occurring affordable housing (NOAH) projects, or Minnesota based impact investing.

The definition of a NOAH property is delegated to the Chief Finance Officer together with the Director of Community Planning and Economic Development. These investments would include mortgage backed securities (MBS) guaranteed by Government Sponsored Enterprises. The

securities purchased with these designated assets must meet the criteria for MBS set within the Minnesota Statute, Section 118A.04 Subd. 2 and Subd. 6. In order to support affordable housing projects, the City acknowledges that these investments may be made at below-market yields. These securities will be reported separately from the rest of the core portfolio.

Minnesota based impact investing (MII) could include affordable housing, small business development and sustainable infrastructure projects within the City that meet the criteria of the Minnesota Statute, Section 118A.04 such as Small Business Administration guaranteed loans, mortgage backed securities (MBS) guaranteed by Government Sponsored Enterprises or Federal Agency securities backed by the full faith and credit of the United States Government. These securities will be purchased at prices consistent with the general market and will have a weighted average life of ten years or less. These securities will be reported separately from the rest of the core portfolio.

The strategy for the *debt service reserve portfolio* is to pro-actively manage these reserves for bonds issued for development. Portfolio structure will consider anticipated needs. The dollar weighted average maturities for securities in this portfolio will generally be within five years unless bond documents dictate a shorter duration. Portfolio managers must adhere to eligible securities, maturity and duration parameters established, and revised periodically, by the applicable bond documents.

V. Authorized Investments

Assets of the City shall only be invested in securities authorized by Minnesota Statute Chapter 118A (Attached).

Additional Restrictions on authorized investments imposed by the City:

The City Council of the City of Minneapolis has resolved to not invest City funds, directly or indirectly, in fossil fuel companies. All investment managers, whether City employees or external managers, shall take care to exclude from the City's investment portfolio(s) under their management, any type of investment securities of such companies. All individuals involved in the City's investment program, including external investment managers, Independent Investment Consultant, Investment Compliance Administrator (ICA) and the Director of Investments Capital and Debt Management (Director of ICDM), shall monitor the portfolio to ensure compliance with the divestment from fossil fuel companies resolution.

VI. Standards of Care

The standard of care to be used by all City investment officials, or their agents, shall be the "prudent investor rule" and shall be applied in the context of managing an overall portfolio. The "prudent investor rule" states that, "*Investments shall be made with judgment and care, under circumstances then prevailing, which investors of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.*"

External SEC-registered investment managers contracted by the City are held to the "Prudent Expert Standard" which considers an anticipated level of required expertise and experience.

VII. Delegation of Authority and Responsibility

CFO, Director of ICDM, ICA

Authority to manage the investment program is granted to the CFO by the City Council and the Minneapolis, Minnesota, Code of Ordinances, Title 2 – Administration Chapter 17.50 and 17.60. The CFO has further delegated the responsibility for the daily operations of the investment program to the Director of ICDM and

the ICA. The CFO and the Director of ICDM shall retain fiduciary responsibility for the portfolio(s). The CFO shall receive monthly and quarterly reports, and ongoing updates on the portfolio as deemed necessary.

Investment Officer

The Director of ICDM shall assume the duties of the primary Investment Officer (IO) and act in accordance with this Policy and the established written Internal Controls and Procedures for Investments. The Director of ICDM delegates the administration of the investment program to the ICA.

All participants in the investment process shall seek to act responsibly as custodians of the public trust. No officer or designee may engage in an investment transaction except as provided under the terms of this Policy and City supporting procedures.

The Director of ICDM and the ICA shall obtain a minimum of sixteen hours of investment training from CFO approved sources every two years.

The Investment Officer and staff involved in the investment process shall refrain from personal activity that could conflict with the proper execution and management of the investment program, or that could impair their ability to make impartial investment decisions.

City Council Responsibilities

The City Council retains ultimate fiduciary responsibility for the portfolio(s). It will receive and review quarterly reports and review and adopt the Investment Policy, as amended from time-to-time, at least every three years.

Investment Managers

The City may utilize SEC registered investment advisory/management firms (External Investment Managers) to invest segments of the portfolio. Managers shall be selected through a RFP process at least every five years. The External Investment Managers will operate within the constraints of this Investment Policy and an executed Investment Management Agreement (IMA).

The External Investment Managers shall have discretion over the assigned segment(s) of the portfolio. The Operating and bond proceeds portfolios however, are constrained by the cash flow needs of the City and related legal covenants. All External Investment Managers shall purchase and sell investment securities on a best execution basis and in accordance with Minnesota Statute 118A and any other applicable legal or statutory requirements, this Investment Policy and the IMA. External Investment Managers may be assigned differing strategies, constraints and assets to manage at the discretion of the CFO and the Director of ICDM. External Investment Managers must be registered under the Investment Advisers Act of 1940 and be licensed and registered to do business in Minnesota and registered as an investment advisor through IARD¹ in Minnesota.

Independent Investment Consultant

The City may utilize the services of independent investment consultant(s) to assist the City in the management, oversight and evaluation of the investment portfolio. The City can use the consultant(s) to monitor the activities of the External Investment Managers and to provide investment reports on the portfolio in addition to the External Investment Manager's reports. The services required of the consultant(s) are detailed in the agreements between the City and the consultant(s).

¹ All institutional investment advisers are registered and regulated by the SEC Securities and Exchange Commission. The IARD (Investment Adviser Registration Depository) is an online system for advisers and investors who want to check the registrations and history on advisers. The State of Minnesota uses the IARD/SEC registration for its own registration requirements so that both stay in step on current information. All advisory information is updated annually.

VIII. Financial Agents

1. Authorized Broker/Dealers

The City and its External Investment Managers may purchase securities directly only through FINRA registered broker/dealers or purchase time and demand deposits through FDIC/NCUA insured financial institutions.

Each authorized broker/dealer from whom the City purchases securities directly must be provided the City's Investment Policy annually and certify receipt and review in accordance with State law. Such firms shall be authorized to provide investment services in the State of Minnesota. These may include "primary"² or regional dealers that qualify under Securities & Exchange Commission Rule 15C3-1 (uniform net capital rule). All broker/dealers who desire to become qualified bidders for investment transactions must supply the Director of ICDM with (if brokers) Financial Industry Regulatory Authority (FINRA³) certification and CRD number. The list of all authorized firms/broker/dealers will be reviewed at least annually by the Director of ICDM and CFO.

Each External Investment Manager must be provided a copy of the City's current Investment Policy and certify to a review of the Policy affirming that only Policy approved investments will be purchased for the City in accordance with Minnesota statutes. External Investment Managers must ensure that broker/dealers whom they transact with on behalf of the City must be authorized and have the credentials described in the preceding paragraph.

Eligible Investment Managers must note the firm on each transaction document.

2. Eligible Depositories

Pursuant to Minnesota Statutes, Section 118A.02, the City Council shall designate one or more depositories eligible to receive city funds. A depository must be a member of the Federal Deposit Insurance Corporation (FDIC) or the National Credit Union Administration (NCUA) and shall collateralize all time and demand deposits daily in excess of FDIC coverage to 110% in accordance with Minnesota Statutes (Section 118A.03 as amended) and Section X of this Investment Policy.

3. Custodian (Safekeeping) Bank

The City selects a Custodian through a competitive process at least every five years for settlement and safekeeping of its securities purchased. The Custodian may be the City's banking services bank. Delivered investments purchased by the External Investment Managers or securities purchased directly by the City shall be held and designated for the City with the Custodian. The Custodian will create a safekeeping account and a cash account or a money market mutual fund account for each External Investment Manager and an account (or sub accounts) for the City's investment transactions. Funds assigned to the External Investment Managers are transferred through the cash account or the money market fund(s) at the City's direction.

IX. Safekeeping and Custody

1. Delivery vs. Payment

All securities trades, made by the City or its External Investment Managers, shall be executed (cleared and settled) on a delivery vs. payment (DVP) basis to ensure City control at all times. The designated banking services depository may be used as the City safekeeping agent (custodian) for all securities to eliminate unnecessary transfers and possible delays in execution. The City will retain control of its funds and its assets at all times. The City may also invest funds with investment providers, approved by the City Council, who hold securities in custody on behalf of the City.

² "Primary" dealers are designated and regulated by the Federal Reserve Bank of NY.

³ FINRA is the self-regulatory national organization for broker/dealers. All registration and certification information is kept in their Central Registration Depository (CRD) which is available online to all investors.

The safekeeping agent will provide, on request by the City, a safekeeping receipt for each City owned security and a monthly descriptive report of all City holdings. The safekeeping agent shall annually provide a copy of its most recent report on internal controls to the Director of ICDM. These Service Organization Control Reports shall be prepared in accordance with the Statement on Standards for Attestation Engagements (SSAE) No. 16.

To perfect the required delivery versus payment (DVP) settlement process, the Custodian (or safekeeping agent) will not be used as a broker/dealer. A brokerage subsidiary affiliate of the Custodian must be able to clear and settle all security trades on a delivery vs. payment (DVP) basis⁴ between legally separate entities in order to be used considered as an authorized broker/dealer.

2. Custody of Pledged Collateral

An independent, third-party custodian for collateral pledged to the City for all time and demand deposits may be designated by the pledging bank and approved by the CFO by entering into a pledged collateral agreement. Collateral for deposits will be pledged to the City as evidenced by safekeeping receipts from the institution with which the collateral is deposited. The custodial bank will be outside the holding company of the pledging bank. Original safekeeping receipts shall be obtained in a timely manner and reports of the pledged collateral will be received monthly from the Custodian.

X. Collateralization

Full collateralization will be required on all time and demand deposits in accordance with Minnesota Statutes, Section 118A.03.

Acceptable collateral for all time and demand deposits which are pledged to the City shall be:

- margined to 110% of deposited funds plus accrued interest (Minnesota Statutes Chapter 118A.03, Subd. 3).
- marked-to-market at least weekly,
- held by an independent institution outside the holding company of the pledging institution. approved by the City.
- Federal Home Loan Bank irrevocable standby letters of credit

Acceptable collateral which is owned by the City under a repurchase agreement shall:

- be margined at 102%
- be marked-to-market daily by the custodian,
- be held by an independent financial institution outside the holding company of the counterparty and approved by the City, and
- include only, the acceptable forms of collateral for time and demand deposits.

XI. Internal Controls

The CFO and Director of ICDM are responsible for establishing and maintaining the internal control structure to ensure that the cash and investments of the City are protected from loss, theft or misuse. Specific controls and procedures are documented in the City's Internal Controls and Procedures for Investments which shall be reviewed and approved by the Director of ICDM and the CFO and revised as needed.

Internal controls shall be designed to provide reasonable assurance that policy objectives are met. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived and recognizes the valuation of costs and benefits requires estimates and judgments by management. The internal controls shall address the following points at a minimum:

- Control of collusion by independent account reconciliations

- Separation of transaction authority and transactions processing
- Custody and safekeeping
- Clear delegation of authority
- Documentation of all transactions
- Dual authorizations of wire transactions and transfers
- Staff training
- Review, maintenance and monitoring of security procedures both manual and automated.

The internal controls may be reviewed by the internal auditor and the external auditor as designated by the CFO.

Downgrades:

Credit ratings on all securities shall be monitored on no less than a weekly basis by the External Investment Manager(s). If the required credit rating of a security owned by the City is downgraded below the minimum rating level required by the State or Policy, the External Investment Manager(s) shall immediately inform the Director of ICDM of the downgrade action and within three days provide an evaluation of the action to be taken based on the conditions affecting the rating, possible loss of principal, and liquidation options available. The External Investment Manager(s), with the Director of ICDM, will apply the general objectives of safety, liquidity, yield and legality to make a decision on liquidation alternatives.

Monitoring FDIC Status

External Investment Managers holding brokered CDs shall monitor, on no less than a weekly basis, the status and ownership of all banks issuing brokered CDs owned by the City based upon information from the FDIC. If any bank has been acquired or merged with another bank in which brokered CDs are also owned, the External Investment Manager shall immediately liquidate any brokered CD which places the City above the FDIC insurance level. CDs may be held in amounts in excess of FDIC insurance if the CDs are collateralized by eligible collateral or irrevocable standby letters of credit issued by Federal Home Loan Banks to the City.

XII. Reporting

The City’s External Investment Managers shall provide the City and its Custodian monthly reports on their managed portfolios. The reports are prepared in accordance with the City’s specifications, communicated to the External Investment Managers in writing, and are available in the month following the reporting period, on a date agreed to by the City and its External Investment Managers.

The City’s Custodian shall submit a monthly investment report for each External Investment Manager as well as for the internally managed Operating account. In addition, the Custodian shall provide a combined report of all External Investment Managers and the Operating account, to the Director of ICDM in the month following the reporting period, on a date agreed to by the City and the Custodian. The reports shall be prepared in accordance with the City’s specifications and be communicated to the Custodian in writing.

No less than monthly, the Director of ICDM shall present to the CFO a comprehensive cash and investments report. On a quarterly basis, the report will mark the portfolio to market and contain a brief summary of current economic conditions affecting the portfolio. A cash and investment report is also presented to the Ways and Means Committee of the City Council along with the Controller’s financial report on a quarterly basis.

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