Winnipeg

Reserves Administration Audit

Final Report
December 2006

Audit Department

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Executive Summary

Reserves are funds that have been set aside for designated purposes; prudent administration of reserves represents an important component of sound financial management. Maintaining adequate reserves provides the City with the ability to respond to unexpected events, maintain stable taxes, and ensure that sufficient funds are available for major capital projects. Reserves can only be created with Council approval.

Reserves represent a significant financial asset for the City. In 2005, the balance in the reserves was approximately $292 million, which is equal to 28% of the City's budgeted expenses for the year.

The City classifies reserves into three categories:

- Stabilization reserves – these are established to deal with unanticipated fluctuations in revenues or expenditures.
- Capital Reserves – these are established to maintain funding for capital projects in order to reduce the amount required to be financed by new debt.
- Special purpose Reserves – these are established to fund specific program needs.

The Reserves Administration Audit was included in our 2004 – 2006 Audit Plan. The objectives of the audit were as follows:

- To determine whether appropriate fund limits have been established for selected reserve funds.
- To determine whether fund balances have been invested appropriately.
- To evaluate whether reserve fund transactions were in compliance with the appropriate by-laws and Council minutes.

Our audit testing was focused on five specific reserves, but we also made some observations that applied to all reserves. A summary of our more significant observations is captured below:

Significant Observations

We compared the City's practices relating to the administration of reserves to a list of "best practices" developed by a specialist retained to assist us with our review. Overall, we are pleased to report that the City's practices incorporated the majority of practices noted. In this regard, several strengths were identified.

For the reserve funds that we reviewed, the fund targets appear to be sufficient to meet the intended objectives. In instances where actual balances differed from the target, fund managers had identified the surpluses or deficits associated with their reserves. In addition, the reserve funds are being managed by the City Treasurer's Division and fund managers in adherence to the appropriate by-laws and Council resolutions.

The City Treasurer's Division, working within the parameters of the *City of Winnipeg Investment Policy,* has been able to achieve investment performance on the reserve funds that is consistent with accepted industry benchmarks. We did identify, however, an opportunity for fund managers, in consultation with the City Treasurer's Division, to derive better rates of return by segregating reserve funds into short-term and long-term components, depending upon cash flow requirements. Our analysis, using 2005 data, estimated that the opportunity cost of not allocating the idle portions of the pooled reserve funds to longer-term investments ranged from $38,000 to $171,000.

We compared the City's *Investment Policy* to guidance provided by The Office of the Superintendent of Financial Institutions Canada and to the investment policies of two of the municipalities surveyed by our

specialist. We noted that, in general, the City's policy is consistent with the guidance and similar to the other cities but could be strengthened by incorporating expectations and standards for performance as well as formal reporting requirements.

We also observed that the City's investment strategy is more conservative than the other cities surveyed. While we endorse the City's goal of preservation of principal, we noted that increasing our risk tolerance by reducing some of the restrictions in the City's *Investment Policy* has the potential to result in better rates of return. An increase of 5 or 10 basis points in the rate of return would result in additional annual earnings of $146,400 to $292,801, respectively, based on 2005 balances.

Currently, the City has no formal policy on internal charges. In the absence of a policy, Council approved an internal charge to the reserve funds for management fees. Corporate Finance has also earned an interest revenue premium on the shorter-term funds invested, in effect, a second fee. We recommend that the CFO review the basis for internal charges for management of the investment portfolio.

With respect to the specific reserves reviewed, we found that, overall, good financial controls were in place to ensure expenditures from the reserves met the intended objectives. However, we also noted that the process to create or amend a reserve and the process to administer a reserve are not formally documented. To ensure continued compliance with the governing documents and to ensure continuity of knowledge of key staff, we have recommended the creation of an administrative directive to provide direction to fund managers regarding the creation and on-going administration of reserves.

Our specialist observed that the level of detail on reserves disclosed in our annual financial statements was superior to the other cities surveyed. Development of performance targets and benchmarks as well as a requirement to report annually to fund managers and Council on the performance of the funds invested would enhance accountability.

A summary of all nine recommendations made in our report can be found in Appendix 10.

Mandate of the City Auditor

The City Auditor is a statutory officer appointed by City Council under the *City of Winnipeg Charter Act*. The City Auditor reports to Council through the Audit Committee (Executive Policy Committee) and is independent of the City Administration. The City Auditor conducts examinations of the operations of the City and its affiliated bodies to assist Council in its governance role of ensuring Civic Administration's accountability for the quality of stewardship over public funds and for the achievement of value for money in City operations. Once an audit report has been communicated to Council, it becomes a public document.

Audit Background

Reserves are an important component of sound financial management and are funds that have been set aside for designated purposes. Maintaining adequate reserves provides the City with the ability to respond to unexpected events, maintain stable taxes, and ensure that sufficient funds are available for major capital projects. Reserves can only be created with Council approval.

Reserve Administration was included in the Audit Department's Audit Plan for October 2005 to October 2006, approved by Audit Committee in 2004.

Audit Objectives

The objectives of the audit were as follows:

- To determine whether appropriate fund limits have been established for selected reserve funds.
- To determine whether fund balances have been invested appropriately.
- To evaluate whether reserve fund transactions were in compliance with the appropriate by-laws and Council minutes.

Audit Approach

We have conducted the audit in accordance with generally accepted auditing standards. **Appendix 1** provides a flowchart of the audit process.

- We conducted interviews with key managers and staff associated with the creation and administration of the reserves to gain an understanding of the process, the roles and responsibilities of specific positions, and to identify potential issues or areas of focus for the fieldwork phase of the review.
- We reviewed related by-laws, Council minutes, reports, policies, procedures and other relevant background documentation related to the administration of the reserves.
- We retained an investment specialist from Deloitte & Touche LLP to ascertain how selected other cities (Ottawa, Hamilton, Calgary) administer reserves, to identify benchmarks for performance and to suggest best practices for reserve administration. The Terms of Reference are included as **Appendix 2**.
- We selected five reserves for detailed review and drew a sample of transactions to test for compliance with City by-laws, Council minutes and other internal guidance. Our review period was 2003 to 2005, inclusive. (See **Appendix 3** for details regarding the sample.)
- At the conclusion of the audit, we provided a report to management, Senior Administration and Council.

The conclusions in our report are based upon information available at the time. In the event that significant information is brought to our attention after completion of the audit, we reserve the right to amend the conclusions reached.

Audit Conclusions

The audit work we performed led us to the following conclusions:

- For the reserve funds that we reviewed, the fund targets appear to be sufficient to meet the intended objectives. In instances where actual balances differed from the target, fund managers had identified the surpluses or deficits associated with their reserves.

- The City Treasurer's Division, working within the parameters of the *City of Winnipeg Investment Policy,* has been able to achieve investment performance on the reserve funds that is consistent with accepted industry benchmarks. At the same time, we identified opportunities to enhance performance through better investment management of certain reserve funds.

- The City Treasurer's Division and fund managers are managing the reserve funds in adherence to the appropriate by-laws and Council resolutions. Established practices, while working well, should be formalized.

Acknowledgement

The Audit Department wants to extend its appreciation to the management and staff from all City departments who participated in the review and, in particular, the managers and staff of the Corporate Finance Department. In addition, we acknowledge the assistance provided by Deloitte & Touche LLP.

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December 2006
Date

Financial Significance of the Reserves

The City maintains 31 reserves. The following table identifies the total dollar value held in those reserves for the years 2003 to 2005 (in thousands of dollars). The reserve balances have been relatively stable over this period. (See **Appendix 4** for a detailed listing of the reserves.)

	2003	2004	2005
Total Reserves*	$295,756	$314,228	$292,801
Operating Budget*	$1,031,425	$1,025,472	$1,044,923
% of Budget	28.7%	30.6%	28.0%

* in thousands of dollars

The City classifies reserves into three categories:

- Stabilization reserves – these are established to deal with unanticipated fluctuations in revenues or expenditures.
- Capital reserves – these are established to maintain funding for capital projects in order to reduce the amount required to be financed by new debt.
- Special purpose reserves – these are established to maintain specific program needs.

Reserve	2003	2004	2005
Stabilization*	$60,588	$62,325	$64,004
Capital*	152,804	179,679	159,772
Special Purpose*	82,364	72,224	69,025
	$295,756	**$314,228**	**$292,801**

* in thousands of dollars

Reserves represent a significant financial asset to the City of Winnipeg and are a critical component of the City's overall financial management strategy. It is essential that these assets are administered and managed in a manner that ensures that the City's financial management objectives can be met.

Overview of the Reserves Administration Process

The City of Winnipeg has two key documents that govern the creation and the administration of all reserves:

- the *City of Winnipeg Charter Act*
- the *City of Winnipeg Investment Policy*

Subsection 289(1) of the *City of Winnipeg Charter Act* (the *Charter Act*) allows the City to establish a reserve for any purpose for which the City has authority to make expenditures. Subsection 289(3) provides parameters for the types of securities where the investment funds may be deposited. Finally, Subsection 289(4) restricts the use of reserve funds to the purpose for which they were originally identified. The section identifies exceptions to the above-noted rule which include

- the amount in the fund is greater than required;
- the amount in the fund is no longer required for the established purpose; and
- the purpose of the fund is terminated.

The *City of Winnipeg Investment Policy* (the *Investment Policy)* provides the City with an approved framework for managing its investment program. The *Investment Policy* states "that unless specifically directed or restricted by Council, the Chief Financial Officer (CFO) determines the investment term of specific reserve funds".

Each reserve is governed by a by-law, or Council minute, or combination of the two. The by-laws or Council minutes usually outline the purpose of the reserve, how the reserve is to be funded, what constitutes a qualified expenditure and identifies the fund manager.

Although there are no formal policies in place regarding the creation of a reserve except for the provisions of the *Charter Act,* the City has established practices for creating a reserve. To create a reserve, a department usually consults with Legal Services and prepares a report, outlining the purpose and identifying the fund manager. This report is submitted to the Chief Administrative Officer (CAO) for approval. The CAO may consult with Legal Services and the CFO prior to endorsing it. The department then submits the report to Council for approval. Reserves are typically created once a year in conjunction with approval of the budget.

Amendments to reserves essentially follow the same process but can occur throughout the year. Legal Services is usually involved to ensure compliance with the *Charter Act.*

Fund managers are typically the heads of the departments responsible for the reserve. The fund managers establish informal funding and expenditure guidelines if not established in the applicable by-laws or Council minutes. The administration of the reserve is usually delegated to a financial professional who ensures proper financial controls are in place to ensure that the appropriate funding is received and that only expenditures consistent with the fund's purpose are made.

The City Treasurer's Division manages the investment of reserve funds. Funds earn a monthly or quarterly investment income depending upon the nature of the reserve and are charged a management fee for this service. The City Treasurer's Division and the fund managers meet at least annually to discuss the investments and cash needs of each reserve.

Key Risks and Impacts Associated with the Administration of Reserves

Risk is defined as any circumstance or event that has an impact on the achievement of business objectives. Accordingly, risk can be either a threat or an opportunity. The failure to seize an opportunity can negatively impact the achievement of business objectives. We assessed the key potential risks associated with the administration of the reserves and the resulting impacts to the City. The key sources of risk associated with the administration of reserves are

- reserve funds are inadequate to meet objectives;
- contributions to reserves funds do not comply with by-laws and Council minutes;
- reserve funds are inappropriately invested and not adequately safeguarded;
- expenditures are not in compliance with Council minutes/by-laws;
- excess funds sit idle in reserves; and
- oversight by the fund manager is inadequate.

The most significant negative impacts that the City may realize when administrating the reserves are

- insufficient funds in a reserve hinders the ability to serve the intended purpose, negatively impacting the delivery of City services;
- less than optimal investment returns result in the use of operating funds to maintain sufficient levels in the reserves;
- expenditures are made out of a reserve that are not consistent with the reserve's purpose:
- excess money exists in reserves but is not used to address operating budget challenges; and

- insufficient reporting of information to fund managers results in their inability to adequately perform their oversight responsibility.

Observations and Recommendations

The City of Winnipeg's administration of reserves is open to scrutiny from a variety of sources. Councillors, citizens and other stakeholders may question the necessity of the reserve or the adequacy of the reserve funding level. This is particularly true in the current environment of budgetary restraint where the Administration and Council are looking for additional sources of funds to meet increasingly tight budgets.

While our audit testing was focused on five specific reserves, we also have some observations that apply to all reserves. These general observations are discussed in the next two sections. Our observations relating to the specific reserves reviewed in depth follow in the final section of the report.

Areas of Strength

We compared the City's practices relating to the administration of reserves to a list of "best practices" developed by our specialist **(Appendix 5)**. Overall, we are pleased to report that the City's practices incorporated the majority of practices noted. Strengths observed included the following:

- The City's overall inventory of reserves appears consistent with the long range financial plan.
- The Administration's practices for the creation of a reserve are consistent with the provisions of the *City of Winnipeg Charter Act*.
- At least annually, the purpose and funding level of each reserve fund is reviewed at a high level.
- Reserve fund targets appear to be sufficient to meet the intended objectives of the reserves we reviewed.
- Individual reserve funds are pooled to maximize investment returns.
- The reserve funds are being managed by the City Treasurer's Division in adherence to the investment parameters of the *City of Winnipeg Charter Act* and the *City of Winnipeg Investment Policy.*
- Fund managers assign responsibility for the administration of a reserve to a finance professional who has developed financial controls to ensure that the reserve funds are adequately administered.
- The investment performance of the reserve funds is consistent with the accepted industry benchmarks for the type of allowable investment securities.
- Reporting in the detailed annual financial statements and five-year cash flow forecasts is sufficient to provide an overview of the use and source of funds for each reserve.

In the next section, we provide our general observations including areas where we identified the need for improvement or opportunities to potentially enhance our investment performance.

General Observations

The overall level of reserves appears to be adequate.
Reserves form a critical component of the City's overall financial management strategy. Reserves are one indicator, of many, in the credit rating assigned by agencies such as Standard and Poor's (S&P), Moody's and Dominion Bond Rating Service. The credit rating affects the interest rate the City can pay when it issues new bonds. A higher credit rating may result in lower costs of borrowing, leaving more funds available for the delivery of City services.

Our specialist compared the City's bond rating, reserve levels and annual expenditures to three other cities. The table below highlights the current bond rating by Standard and Poor's and an analysis of the financial results for the year 2005.

	Winnipeg	Calgary	Hamilton	Ottawa
S&P Long term rating	AA	AA+	AA	AA+
Trend	Stable	Stable	Positive	Stabile
Total Reserves	$292,801	$497,571	$365,071	$451,438
Total Expenses	$958,833	$2,729,985	$1,301,921	$2,317,524
% of Expenses	30.5%	18.2%	28.0%	19.5%

The City's current long-term rating is AA, which is considerably higher that it was 10 years ago. The increased rating has likely translated to lower costs of borrowing, contributing to the City's ability to reduce its total debt load. Any significant negative change to the bond rating could have ripple effects on the City's debt reduction strategies and overall financial plan.

The total value of reserves is the lowest of the three surveyed cities, but this is placed into perspective when the total operating costs are also taken into account. The City of Winnipeg's reserves comprise a higher percentage of total expenses. This means that the City is better prepared to handle major fluctuations in revenue sources, such as property taxes or transfer payments from other levels of government, and in expenditures.

The City's credit rating should remain stable in the absence of any major shift in the City's revenue sources, total debt load, fundamental change in the fiscal management strategy, and elimination of certain key reserves or material reduction of reserve levels in general.

Proper due diligence should continue to be performed regarding the reserves. Annually, fund managers perform a high-level review of each reserve fund to ensure that the purpose is still applicable and the intended level is adequate. Any adjustment to a reserve should be made because a comprehensive analysis suggests the funded level is too high or that the risk associated with the reserve has declined.

Performance expectations and reporting requirements in the City of Winnipeg's Investment Policy should be strengthened.

The stated purpose of the City's *Investment Policy* is to provide the City with an approved framework for managing its investment program. This policy provides direction and an accountability structure for the Corporate Finance Department in the execution and management of investment transactions. The policy forms the foundation for a sound investment program, which, in turn, is a critical component of the City's overall financial management strategy.

Due, in part, to innovations in securities instruments and a vastly more complex investment environment, The Office of the Superintendent of Financial Institutions Canada issued a guideline on securities portfolio management in 1998. The guideline outlined the significant components of both a sound investment management program and sound investment policy. (An excerpt of the guideline is provided in **Appendix 6.**) As a part of the jurisdictional review, our specialist also obtained summaries of the investment policies for the City of Hamilton and the City of Calgary. We compared the City of Winnipeg *Investment Policy* with certain criteria contained in the federal guideline as well as the policy summaries from the other cities. (See **Appendix 7.)**

In general, our policy contained most of the key components recommended by the guideline as well as contained in the policies of the other cities.

Unlike the City of Winnipeg, however, the investment policies for Hamilton and Calgary described performance expectations, benchmarks and reporting protocols. For example, the City of Hamilton's Investment Policy describes portfolio return expectations, performance objectives, and performance measurement benchmarks and requires a detailed annual report to Council on the performance of the City's investment portfolio. The City of Calgary's policy outlines performance benchmarks, standards and reporting requirements. The policies for both cities also require a formal report on a quarterly basis indicating that the management of the funds was in compliance with the investment policy.

The City of Winnipeg policy does not contain performance expectations or reporting requirements. The policy only makes reference to a credit exposure report to be provided to the City Treasurer. There is no requirement to report to Senior Administration or Council; however, in practice, an informal meeting with the CFO is conducted monthly. The City of Winnipeg policy does not require a compliance report to Council.

Clearly establishing expectations for performance as well as a formal reporting protocol would enhance the accountability for the management of the City's investment portfolio. It would also provide the basis for on-going discussions about the effectiveness of the City's investment strategy with fund managers, Senior Management, and Council.

Recommendation 1
We recommend that the Chief Financial Officer conduct a review of the City's Investment Policy with respect to establishing performance objectives, benchmarks and reporting requirements. The results of the review should be communicated to Council with an appropriate recommendation for revisions.

Management Response
As part of the annual review of the City's Investment Policy, the Chief Financial Officer will research and consider performance objectives, benchmarks and reporting requirements, and will recommend appropriate changes be brought to Council for approval.

Changes to the City's investment strategy may provide an opportunity to increase rates of return.
The *City of Winnipeg Charter Act* provides guidance on the investment securities that the City may purchase, acquire or hold. (See **Appendix 8** for relevant excerpts from the *Charter Act*.) The *Charter Act* allows the City to invest in many different types of securities, including those issued by

- government bodies,
- financial institutions,
- municipalities,
- school boards/districts,
- hospitals or health districts funded by the government, and
- corporations belonging to a class authorized by the Minister of Finance.

The *City of Winnipeg Investment Policy* places restrictions on the type of investments that the City Treasurer's Division is permitted to purchase. (See **Appendix 9** for relevant excerpts from the *Investment Policy.*) Securities allowable under the *Investment Policy* include

- government bodies,
- municipalities,
- major Canadian banks, and
- Schedule II banks.

Besides restricting investments that would be allowed under the *Charter Act,* the *Investment Policy* imposes limits on the percentage of a specific type of security that the City may hold. To provide a basis for comparison, we requested our specialist to perform a review of the investment

strategies of Calgary, Ottawa and Hamilton. The review revealed that the City's risk tolerance is lower than the other municipalities. Some examples of the differences include the following:

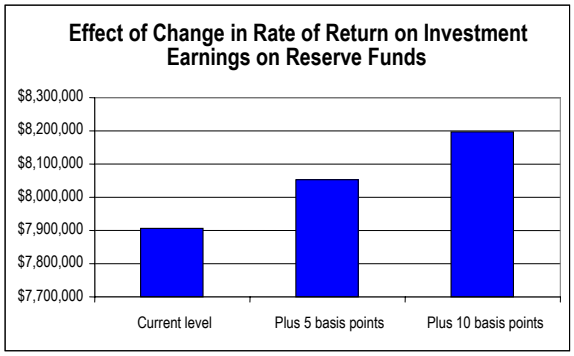
- The other cities are not as restricted in the types of investments that can be held. Unlike Winnipeg, Ottawa and Hamilton can hold corporate securities. Calgary can invest in mortgage backed securities and real estate.
- The credit rating for long-term investments must be "AA" and includes a maximum limit depending upon the term. Other jurisdictions allow for "A" and do not have the same restrictive maximum limit.
- A minimum of 50% of long-term investments must be Government of Canada and Guarantees and a maximum of 25% in other Municipalities. Other jurisdictions are not as restrictive.

We do note that while the investment policies of other jurisdictions do allow expanded investment opportunities, it was beyond the scope of this audit to review their actual investment practices.

A fundamental consideration of the *City of Winnipeg Investment Policy* is preservation of principal: *"Safety of principal is the overriding consideration in investment decisions."* Staff in the City Treasurer's Division have achieved that objective while, at the same time, generating returns that have often exceeded industry benchmarks. Nevertheless, we believe that there is an opportunity cost to maintaining the current investment strategy.

We believe that it would be worthwhile to review the City's investment strategy to determine whether prudent changes to the restrictions placed on investments would allow for increased rates of return while safeguarding fund assets. This review should include a comparison to the strategies of other cities and the relative results achieved. To assist in the review, we have provided the report on the information and analysis compiled by our specialist to the Corporate Finance Department.

In terms of the potential impacts of a change in investment strategy, the graph below illustrates the effect of a 5 or 10 basis point change in the investment earnings of the reserve funds. (One basis point equals one hundredth of one percent.)



The total balance of the reserve funds in 2005 was $292,801,000. A change of 5 or 10 basis points could result in additional annual earnings of $146,400 or $292,801.

A less conservative investment approach creates greater investment flexibility; it also creates greater risk. The upside is that it could potentially lead to improved average rates of return; the downside is that the average rate of return could be reduced.

Recommendation 2
We recommend that the Chief Financial Officer conduct a review of the City's investment strategy. The results of the review should be communicated to Council with a recommendation, if appropriate, to revise the current Investment Policy.

Management Response
As part of the annual review of the City's Investment Policy, the Chief Financial Officer will review the City's investment strategy to determine if opportunities exist to expand the current strategy while maintaining an acceptable level of risk and

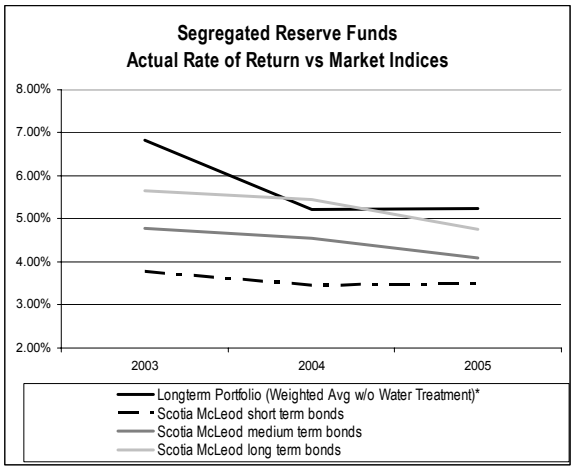
liquidity, and will recommend appropriate changes be brought to Council for approval.

Allocating portions of the pooled reserves between short-term and longer-term requirements could improve the rate of return.

The City currently has 31 separate reserves totalling more than $292 million, classified into three categories: Stabilization, Capital and Special Purpose. The reserves are managed in two ways: segregated basis or a pooled basis.

Segregated funds are reserve funds with assets that are managed separately from other funds. The return received is the actual return earned. These segregated funds are typically invested in longer-term investment instruments, thus earning higher returns. In 2005, $100,911,000 was managed on a segregated basis.

As the graph below indicates, the rate of return earned for the segregated reserve funds by the City Treasurer's Division exceeded all indices, with the exception of the Long Term Index in 2004.



A pooled basis is used to combine several funds, usually invested in shorter-term instruments. The City Treasurer's Division combines these funds with operating funds in conjunction with the City's cash management practices. All excess cash is invested in a variety of money market vehicles. The weighted average investment term of these instruments varied between 38 to 43 days over the period of review. The average for 2005 was approximately 43 days. The pooled funds are paid a return equal to the average monthly overnight rate (defined as the interest rate at which major financial institutions borrow and lend one-day funds among themselves) applied to their average monthly balance. This has provided a better rate of return than if each reserve fund was invested independently.

In 2005, $191,890,000 was managed on a pooled basis. Not all of these reserve funds are required in the short term; some of the funds may not be required for months or years. Despite some longer-term requirements, all of the funds are being invested on the premise that the fund manager will need to access 100% of the available funds at any given point in time. This strategy limits the ability of the City Treasurer's Division to maximize the return on these reserve funds.

For the City Treasurer's Division to be able to take advantage of better rates of return typically available on longer-term securities, the requirements of the reserves must be analyzed and portions allocated between longer-term and short-term needs. If the fund managers were able to allocate this money into different portfolios, the City Treasurer's Division would be able to invest some of these funds over the longer-term and earn greater returns.

Every year the pooled reserve funds receive funding, based on reserve specific pre-defined formulae, and have expenditures charged against the balance. The largest outflow of expenditures, during the 2003 to 2005 review period, was in 2005 and accounted for 33% of the entire pooled reserve funds balance. (This does not take into account any contributions to the reserves.)

The largest net outflow (contributions less expenditures) for the reserve portfolio was only approximately 7% in 2005. This means that approximately 93% of the pooled reserve funds balance may have been available for longer-term investment. By investing a larger portion of funds and/or increasing the investment term, there would be incremental increases in the rate of return.

As an example, the table below illustrates a conservative analysis of the potential incremental return of investing half of the funds of the pooled reserve balance with a longer-term outlook ($191,890,000/2 – rounded down to $95 million). The potential difference in the average rates of return is from 4 to 18 basis points, without introducing any incremental credit risk.

	2005 Rates of Return		
	Actual	Blended 6 month T-bill	Blended 1 year T-bill
Rate*	2.69%	2.73%	2.87%
Interest Earned	$2,555,500	$2,593,500	$2,762,500
Potential Incremental Returns	$0	$38,000	$171,000
% Increase	0%	1.5%	6.7%

* Source: Bank of Canada Average Monthly T-Bill Rates

Presently, the securities market is in an inverted yield curve position. This means that short-term investments may earn a greater return than a long-term investment. This is likely a temporary situation and, when the market returns to a normal yield curve, the City would be in a position to take advantage of higher yielding, longer-term securities.

Recommendation 3

We recommend that as part of the City Treasurer's annual review of each reserve with the fund manager, an emphasis be placed on segregating the reserve's cash requirements into short-term, medium-term and long-term components. The recommended investment strategy should attempt to maximize the rates of return in the given market conditions through an appropriate mix of short and longer-term investments.

Management Response

The City Treasurer's annual review of each reserve with the fund manager will include a discussion with respect to segregating the reserve's cash requirements into short-term, medium-term and long-term components. An appropriate investment strategy which considers both risk and return elements will be employed for each segmented portfolio.

An administrative directive should be created to formalize current practices.

Subsection 289(1) of the *City of Winnipeg Charter Act* provides general guidance for the creation of a reserve, requiring a Council resolution. The Administration has established a process whereby a department will submit a report outlining the intended purpose of a reserve and identifying the fund manager. The report will be forwarded to the CAO, who may consult with Legal Services and Corporate Finance, if needed. The report will then go forward to Council, often as part of the budget process.

Once a reserve fund has been created, fund managers and their delegates have developed practices to ensure that the reserve funds are adequately administered. This encompasses ensuring that adequate documentation is maintained for funding the reserve, making expenditures from the reserve, and providing a year-end reconciliation of the reserve balance.

During our audit, we noted some instances where the documentation pertaining to some reserves was contained in a combination of several documents spanning numerous years that were not always easy to locate. In other instances, we were unable to obtain documentation to support the revised objective for a reserve or the rules (funding formula/expenditure guidelines) pertaining to a reserve. This lack of formal documentation creates uncertainty

and could result in reserve funds being used inappropriately. Formally documenting the administrative practices, including defining roles and responsibilities, would mitigate this risk.

Recommendation 4
We recommend the Chief Financial Officer create an administrative directive, for approval by the CAO, to communicate the process and documentation standards required for the creation, amendment and ongoing administration of a reserve.

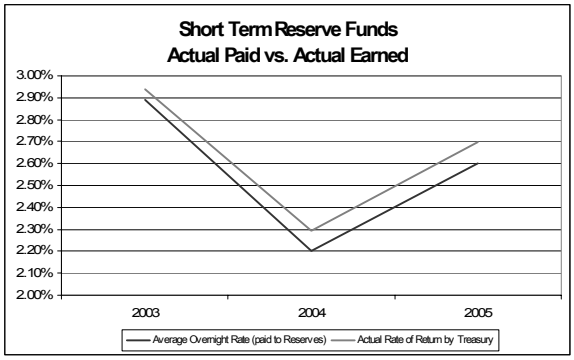
Management Response
The Chief Financial Officer will undertake to draft an administrative directive for approval by the Chief Administrative Officer, to deal with the creation, amendment and administration of the City's reserves.

The basis for Corporate Finance charges for the management of the investment portfolio should be reviewed.
In June 2005, the *Final Report of the Mayor's Red Tape Commission* recommended the creation of a policy on interdepartmental charges. In part, Recommendation 23 stated, "Adopt policies to ensure that internal financial charges are fairly priced…" It is our understanding that the Administration plans to address this recommendation in a report to Council at a future date.

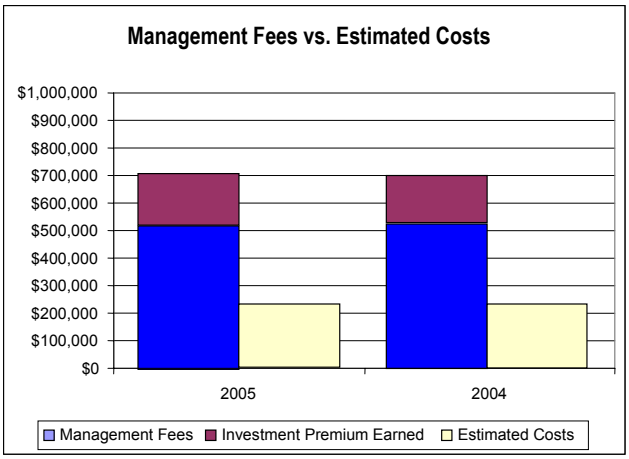
In a report accompanying the 2004 Operating Budget submission, the Chief Financial Officer recommended that a management fee be charged to the reserves for the management of those assets. The Corporate Finance Department's operating budget was reduced by an amount roughly equivalent to the anticipated management fee recovery. The rate recommended was 20 basis points for short-term reserves and 10 basis points for longer-term reserve funds. Part of the rationale for the recommended rate was an informal estimate Corporate Finance received from an external company to provide this service for 25 basis points.

According to the 2005 financial statements, the management fees charged for all reserve funds totalled $522,000. Through discussions with the City Treasurer's Division staff, we estimated that the actual cost incurred for the management of the reserve funds (including salaries, benefits, and overhead) was approximately $250,000 annually.

The City Treasurer's Division also derives revenue from the spread between what the pooled reserve funds actually earn and what is paid to the reserves. The following graph illustrates the difference between the overnight rate paid to the pooled reserve funds and the actual return earned. The spread averages 5 to 10 basis points and, based on 2005 figures, amounts to between $95,945 and $191,890 annually. In effect, this represents a second fee charged to the reserve funds.



The table below illustrates the difference between the estimated costs incurred to manage the investments and the total amount retained from investment earnings made on the reserve funds in 2004 and 2005. What this means is that a portion of the income earned on reserve funds is being used for a tax-supported internal service rather than to increase funds available for the purposes specified for the reserves.



We believe that internal charges should be transparent and supportable. Business units utilizing internal charges should be able to explain to their clients the basis for the charge and, in particular, the rationale for fees that exceed the cost of the service provided. We recognize that there are valid reasons for an additional charge, for example, to fund research or to acquire specialized software to deliver the service. Clients should be satisfied that fees charged are legitimate expenses that relate to the value of the service provided.

In this case, the current model for internal charges has the benefit of ease of implementation. We agree that this is an important consideration. Fund managers are also aware of the two charges although they may not be aware of the total amount paid each year for the investment of their funds. Nevertheless, it is not entirely clear why investment income earned in excess of actual costs incurred by Corporate Finance to deliver this service would not be more appropriately allocated to the related reserve fund. The rationale for this decision should be reviewed.

Recommendation 5
In conjunction with development of a proposed policy on internal charges, we recommend that the CFO review the basis for the fees charged to reserve funds for management of the investment portfolio.

Management Response
As part of the annual review of fees and charges at the City, the Chief Financial Officer will continue to review the investment management fees charged to reserves, and once a policy with respect to internal charges has been developed and approved, ensure compliance.

Performance reporting on reserve funds invested needs to be improved.
The annual detailed financial statements provide information on the purpose of the reserve and the expenditure guidelines, and identify the fund manager, fund balance and inflows (including investment income) and outflows from the reserve. Our specialist observed that the level of detail with respect to reporting on reserves within the financial statements provided by the City was superior to that of the other cities surveyed.

At least annually, staff from the City Treasurer's Division meet with fund managers to discuss upcoming cash flow projections and the actual rate of return earned by a reserve in the prior period. There is no discussion of performance targets or benchmarks for the upcoming period. In the absence of established performance targets or benchmarks, there is no basis against which the fund manager can evaluate performance.

The jurisdictional survey revealed that both Hamilton and Calgary required regular (at a minimum, annual) reporting on the performance of the reserve funds in comparison to accepted benchmarks. We noted that both cities identify various Scotia Capital indices to benchmark reserve performance. The target benchmark should be reflective of the reserve fund's asset mix. Both the targets and actual performance are shared with the fund managers and reported to Council.

This level of reporting allows fund managers to monitor the investment performance of their reserve funds and to see the

incremental gains in the rates of return received by segregating short-term and longer-term cash requirements. It also allows the City Treasurer's Division to demonstrate that reserve funds have been optimally invested within the parameters of the City's policy.

Recommendation 6
We recommend that the City Treasurer's Division report on the performance of the reserve funds annually to the fund managers and Council. The performance should be compared to portfolio targets that were mutually agreed with fund managers, based upon acceptable industry benchmarks.

Management Response
As part of the annual review process of each reserve, the City Treasurer's division will discuss the performance of the reserves with the fund managers, including comparisons to appropriate benchmarks. Consideration will also be given to including information on the investment performance of the reserves in the City's financial statements.

Observations Related to Specific Reserves

Workers Compensation Reserve

Stated purpose, funding guidelines and expenditure guidelines have not been formally amended to reflect the reserve's current purpose.
The Workers Compensation reserve was originally set up by a by-law in 1918 and amended in 1938 and 1946. The purpose of this reserve was to cover the costs associated with workers compensation claims. In effect, the City is acting as a self-insured organization.

In 1983, a report to the former Board of Commissionaires made several recommendations to overhaul the administrative practises related to workers compensation claims. At some point after that report was issued, the purpose of the reserve changed from processing all workers compensation claims to only dealing with fatality claims. Current practice is for general workers compensation claims to be paid from each department's operating budget (i.e. in lieu of salaries).

Although all necessary parties are aware of this revised purpose, the by-law has not been formally amended to reflect the current purpose of the reserve.

Recommendation 7
We recommend that the Chief Financial Officer submit a report to Council, requesting an amendment to the Workers Compensation Reserve to reflect its current purpose as a fatality reserve. The report should also recommend repealing the existing by-law.

Management Response
The Chief Financial Officer will be submitting a report to Council with respect to any recommended changes related to the administration of the Worker's Compensation Reserve.

Perpetual Maintenance Reserve – Brookside Cemetery

A business plan to evaluate the most appropriate business model and/or funding strategy needs to be developed.
The purpose of this reserve is to ensure the perpetual care and maintenance of Brookside Cemetery. Funding for the reserve comes from 25% of the sale proceeds of plots/graves and 50% of the interest earned on the reserve funds. The remaining 50% of the interest earned in the previous year plus 75% from the sale proceeds of plots/graves are applied to the annual operating costs.

Industry best practice indicates that the ideal level for a cemetery perpetual

maintenance reserve can be calculated by taking the annual care and maintenance costs and dividing them by the average rate of return. Using 2005 figures, this would mean that the reserve should be approximately $18 million, which is almost $8 million more than the current balance. The current shortfall is due primarily to a significant reduction (almost 50%) in the interest earned on its reserve balance. A major portion of the reserve funds was invested in high yielding bonds that matured and had to be replaced with lower interest bonds. The shortfall in the reserve level means that supplemental funding for the cemetery's operations must be funded through the City's operating budget. We note that the required funding level for the reserve fund is subject to change with fluctuations in the rate of return and increases in the occupancy rate of the cemetery.

In 1991, a report was forwarded to the Executive Policy Committee that analyzed the options available to the City in terms of maintaining responsibility over the operations of its cemeteries. At that time, a recommendation was made to continue to operate this service.

The Cemeteries Administrator is currently working on developing a business plan for the operation of the City's cemeteries. In light of the significant changes that have occurred between 1991 and the present, the business plan should address which business model would be the most appropriate for the cemeteries service, prior to the Brookside Cemetery reserve receiving increased funding.

If the recommendation is to retain the service, then the business plan should include an analysis of alternative funding arrangements for cemetery operations including the funding of the reserve.

Recommendation 8
We recommend that the Cemeteries Administrator include in the business plan an evaluation of alternative business models for the cemeteries. In addition, and, if applicable, the plan should include a detailed evaluation of the adequacy of the level of the reserve and a plan to ensure the reserve reaches an adequate funding level.

Management Response
The Cemeteries Administrator will ensure a business plan is prepared for the Cemeteries Branch that will examine, among other issues, the adequacy of each municipal cemetery's Perpetual Maintenance Fund to meet the requirements for which they were established.

Fiscal Stabilization Reserve

The process involving the deposit of property taxes collected in relation to the sale of City property needs to be reviewed.
Currently, there is a process in place, administered by staff at the Planning Property & Development Department that involves the collection of property taxes through the Statement of Adjustment when City lands are sold. Current practice is that these tax amounts are collected and deposited in the Fiscal Stabilization Reserve.

These funds should be deposited into the General Revenue Fund to allow for a more accurate calculation of net supplemental taxes received. Net supplemental taxes is the amount of property tax identified as outstanding for a given portion of the year when City land is sold. This amount is estimated and budgeted for by the Corporate Finance Department. By not recording the property taxes in the General Revenue Fund, the amount of net supplemental taxes actually received is understated.

Although this change in the process will not change the total funding the reserve

receives, it will result in better information upon which to base budget estimates for net supplemental taxes. We understand that Taxation and Revenue Branch staff are in the process of recommending a revision to the current process.

Recommendation 9
We recommend that the City Treasurer, as fund manager, revise the current administrative procedure such that the property taxes collected from the sale of City land be deposited in the General Revenue Fund.

Management Response
The City Treasurer has initiated a review of the administrative procedure on property taxes collected from the sale of land to determine if any changes are required.

General Purpose Reserve

During the course of our audit, we observed that the financial controls and processes related to this reserve were satisfactory.

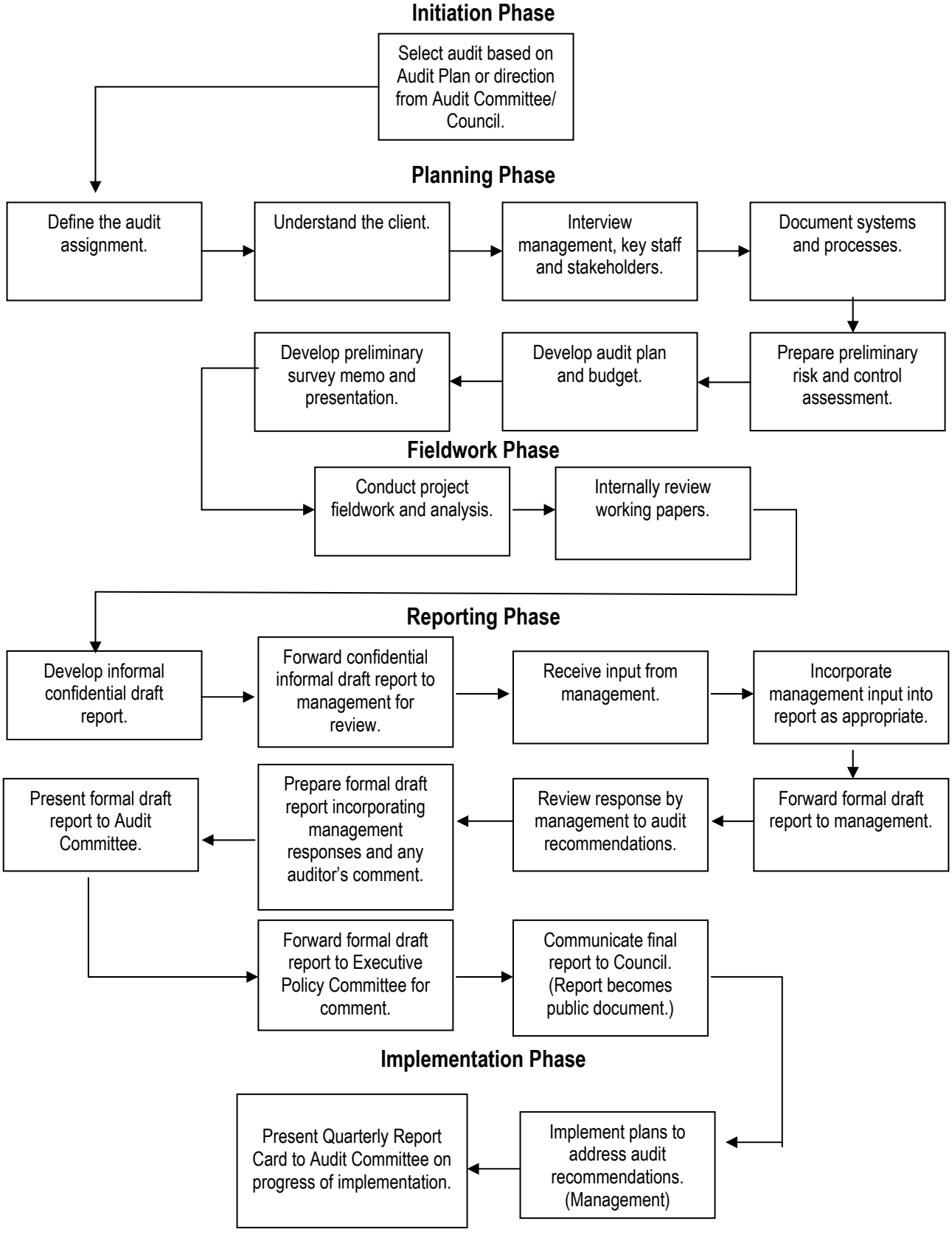
Combined Sewer Renewal Reserve

During the course of our audit, we observed that the financial controls and processes related to this reserve were satisfactory.

Summary of Recommendations

A summary of the recommendations related to the above observations can be found in **Appendix 10.**

Appendix 1: Audit Process



Appendix 2: Specialist Terms of Reference

The Audit Services to be provided on the Reserves Administration Audit are as described below:

I. PERFORM A JURISDICTIONAL COMPARISON - Comparison of City of Winnipeg reserve structure to at least 3 other Canadian Municipalities. The specific municipalities should include Calgary, Ottawa and Hamilton but are negotiable depending upon the availability of relevant information. The criteria for comparison should include at a minimum the following:

- Total revenue and expenses of municipality
- Type of reserves (i.e. reserves or reserve funds)
- Number of reserves
- Dollar amount in each reserve
- Average rates of return on reserve funds
- Composition of reserve balance (i.e. are the reserves or reserve funds made up of liquid assets or capital assets?)
- Method of disclosure for reporting reserves/reserve funds on the financial statements
- Level and basis for management fees charged to reserves
- Excerpts of the critical elements of policies and procedures related to administrating reserves
- Investment strategy restrictions or investment instruments for reserves
- Administration of the reserves - internally or externally managed and degree of oversight (if internal - division of roles and responsibilities between corporate and departmental level for administering, monitoring and reporting on reserves)
- Overview of the process to create a reserve

II. ADEQUACY OF RESERVE LEVELS
- Sensitivity of the City's bond rating to changes in the level of a single or multiple reserves
- Sensitivity of City's insurance costs/rates to changes in the level of a single or multiple reserves

III. BEST PRACTICES
- For the initiation, on-going management and reporting of reserves in municipal government

Appendix 3: Overview of the Sampling Process

Prior to selecting specific reserves to review the Audit Department conducted extensive interviews and gathered internal and external documentation to enhance our understanding of the various types of reserves.

As a result, we developed the following criteria to select specific reserves for review:

- size of the reserve balance,
- reserve from each category of reserve,
- departmental coverage, and
- extent of judgment involved relating to approving expenditures.

The table below illustrates the specific reserves selected for review, the department responsible for oversight and the coverage our sample represents of the total value of all reserve funds. In terms of dollar value, the five reserves we selected represented approximately 30% of all reserve fund balances.

	Fund Manager	Balance ('000s)
All Reserves		
Total – Sample		$88,860
Total - Population		$292,801
Audit Coverage		30%
Stabilization Reserves		
Fiscal Stabilization	City Treasurer	$35,350
Total Stabilization		$64,004
Audit Coverage		55%
Special Purpose Reserves		
General Purpose	City Treasurer	$13,244
Perpetual Maintenance - Brookside	Director PP&D	$9,891
Workers Compensation	Corporate Controller	$6,887
Total - Sample		$30,022
Total -Special Purpose		$69,025
Audit Coverage		43%
Capital Reserves		
Combined Sewer Renewal	Director Water and Waste	$23,488
Total - Capital		$159,772
Audit Coverage		14%

Our review covered a three-year period, 2003 through to 2005. We selected the specific reserve transactions through a manual, random process. Since the sample was based upon judgment, we were unable to extrapolate our observations to the entire value of all reserve funds. We were able, however, to identify issues for further review.

Appendix 4: Details of Reserve Balances

Capital Reserves	Fund Manager	2003*	2004*	2005*
Water Treatment	Director of Water & Waste	$79,073	$93,191	$73,680
Environmental Projects	Director of Water & Waste	39,175	51,230	52,336
Combined Sewer Renewal	Director of Water & Waste	21,917	25,132	23,488
Brady Landfill Rehabilitation	Director of Water & Waste	1,576	1,845	2,114
Golf Course	Director of Planning, Property & Development	1,683	1,714	1,773
Water main Renewal	Director of Water & Waste	1,391	2,005	1,710
Library	Director of Community Services	3,199	1,821	1,477
Computer Replacement	Corporate Controller	1,143	1,092	1,413
Wastewater Sewer Renewal	Director of Water & Waste	452	593	861
Aqueduct Rehabilitation	Director of Water & Waste	1,949	857	457
Transit Bus Replacement	Director of Transit	1,147	89	359
Concession Equipment Replacement	Director of Community Services	99	110	104
		$152,804	**$179,679**	**$159,772**

Stabilization Reserves	Fund Manager	2003	2004	2005
Fiscal Stabilization	City Treasurer	34,246	$34,712	$35,350
Mill Rate Stabilization	City Treasurer	26,342	27,613	28,654
		$60,588	**$62,325**	**$64,004**

Special Purpose Reserves	Fund Manager	2003	2004	2005
General Purpose	City Treasurer	$16,923	$14,060	$13,244
Perpetual Maintenance Fund – Brookside Cemetery	Director of Planning, Property & Development	9,282	9,523	9,891
Heritage Investment	Director of Planning, Property & Development	8,723	8,888	8,744
Insurance	Corporate Controller	7,145	6,721	7,340
Workers Compensation	Corporate Controller	5,605	6,146	6,887
Land Operating	Director of Planning, Property & Development	6,697	5,920	5,975
Commitment	Chief Financial Officer	5,247	4,174	4,310
Contributions in Lieu of Land Dedication	Director of Planning, Property & Development	2,405	2,914	4,130
Economic Development Investment	Director of Planning, Property & Development	5,608	5,474	3,225
Housing Rehabilitation	Director of Planning, Property & Development	1,849	1,138	1,304
Assiniboine Park Enterprise	Director of Community Services	1,031	1,164	1,226
Idea Bank	Corporate Controller	1,497	1,336	907
Multiple-Family Dwelling Tax Investment	Director of Planning, Property & Development	-	250	530
Perpetual Maintenance Fund – St. Vital Cemetery	Director of Planning, Property & Development	507	547	588
Perpetual Maintenance Fund – Transcona Cemetery	Director of Planning, Property & Development	355	381	411
Recreation Programming	Director of Community Services	329	316	313
Snow Clearing	Director of Public Works	9,161	3,272	-
		$82,364	**$72,224**	**$69,025**

* numeric values are in thousands of dollars.

Appendix 5: Suggested Best Practices

Each of Winnipeg, Hamilton, Ottawa and Calgary follow somewhat similar practices with respect to reserve fund management. No one city stood out as having an approach that was demonstrably superior to that followed by others. Nevertheless, in talking to administrators from each of the four cities we found examples of best practices that would include:

- an overall reserve fund policy consistent with the long range city plan;
- reserves supported by complete documentation as to purpose, approval, management, results, reporting and review;
- clear policies with respect to reserve fund oversight, management, control and reporting;
- full public disclosure with respect to the above;
- periodic review of reserve fund purpose and performance and alignment with both operating and capital objectives;
- pooling of individual reserve funds for investment purposes to maximize returns and best use of internal investment expertise;
- establishment of reserve fund investment return objectives and external benchmarks within legislative and policy guidelines;
- using third party fund managers to manage the reserve fund investment program if investment expertise is not available within the city administration;
- reviewing best practices of other municipalities and comparing them to ones used by the city; and
- communication of reserve fund management approach as part of discussion with rating agencies on city financial position and long range plan to maximize rating and reduce borrowing costs.

Appendix 6: Excerpt from the Office of the Superintendent of Financial Institutions Canada

Standards of Sound Business and Financial Practices – Securities Portfolio Management (February 1998)

Managing the securities portfolio is a fundamental component in the safe and sound management of a company. Sound securities portfolio management involves prudently managing the risk/reward relationship and controlling securities portfolio risks across a variety of dimensions, such as quality, portfolio concentration/diversification, maturity, volatility, marketability, type of security and need to maintain adequate liquidity.

Although the particulars of securities portfolio management will differ among companies depending upon the nature and complexity of their securities activities, a comprehensive securities portfolio management program requires:

- establishing and implementing sound and prudent policies to effectively manage the securities portfolio, securities activities and position risk;
- developing and implementing effective securities portfolio management processes governing securities investment decision-making and authority; and
- developing and implementing comprehensive procedure to effectively monitor and control the nature, characteristics, and quality of the securities portfolio and the extent of position risk assumed.

The foundation of an effective securities portfolio management program is the development and implementation of clearly defined policies, formally established in writing, that set out the securities portfolio management objectives of the company and the parameters under which securities activities are to be undertaken and controlled.

Each company needs to establish explicit and prudent securities portfolio management objectives governing:

- the extent to which the company is willing to assume position risk;
- general areas of securities activities in which the company is willing to engage or is restricted form engaging, including the company's policy with respect to acquiring securities of related parties;
- minimum quality and rate of return expectations for the securities portfolio;
- the selection of securities dealers and other counterparties with whom the company is authorized to deal or is restricted from dealing with; and
- securities portfolio concentration and exposure limits

Securities portfolio management objectives reflect a company's risk philosophy, codify investment criteria, establish a foundation for the development of securities portfolio management strategies, and provide the basis for monitoring characteristics and measuring portfolio performance. Securities portfolio objectives provide overall parameters governing securities investment decisions by describing the broad purpose and goals of securities investments. Securities portfolio objectives assist in ensuring that securities are sound and prudent, and that the securities portfolio risk is acceptable given the expected return.

Appendix 7: Comparison of Surveyed Cities Investment Policies

Policy Component	Winnipeg	Hamilton	Calgary
Purpose/Background	Yes	Yes	Yes
Objectives	Yes	Yes	Yes
Delegation of Responsibility	Yes, high level	Yes, detailed	Yes, detailed
Ethics and Professional Conduct	Yes	Yes	Yes
Investment Criteria	Yes	Yes	Yes
Investment Limits	Yes	Yes	Yes
Performance Standards/ Benchmarks	No	Yes, performance against benchmarks and targets reported at least annually to Council	Yes, performance against benchmarks and targets (not clear who receives the report)
Performance Reporting	Yes, partial	Yes, against benchmarks and targets	Yes, against benchmarks and targets
Compliance Reporting	Yes, partial - credit exposure report to City Treasurer	Yes, signed quarterly report from CIO to Council and Treasurer that investment portfolio in compliance with Policy	Yes, signed quarterly report by investment managers (not clear who receives the report)
Downgrades in Credit Quality	Yes, must dispose of investment without compromising portfolio but no written report required	Yes, CIO must submit formal written report on actions to be taken required within ten days, immediately put on Watch List subject to monthly review by Treasure	Yes, must sell the investment within reasonable time considering market conditions
Investment Policy Review	Yes, annual informal review and formally once each Council term	Yes, annual formal review, report to Council	Yes, annual formal review, report to Council
Safekeeping and Custody	Yes	Yes	Yes

Appendix 8: Excerpt from the *City of Winnipeg Charter Act*

List of Allowable Investments

Reserve funds

289(1) Council may provide for the establishment or maintenance of a reserve fund for any purpose for which the city has authority to make expenditures.

Definition of "financial institution"

289(2) In subsection (3), "financial institution" means a bank, trust company, loan company, credit union, insurance company or other similar institution that is supervised or examined by a government or a government authority in the jurisdiction in which it carries on business.

Investment of reserve funds

289(3) Money allocated to a reserve fund established under subsection (1) shall be deposited as provided in clause 100(b) (duties of chief financial officer) and may be used to purchase, acquire, or hold

(a) securities issued by

(i) the government or a government agency,
(ii) the government of Canada or a province of Canada other than Manitoba,
(iii) a government of a country other than Canada or a government of a political subdivision of a country other than
Canada,
(iv) a financial institution,
(v) a municipality, school board or school district in Manitoba, or
(vi) a hospital, hospital district, health district, health and social services district, personal care home or other related or similar entity funded directly or indirectly out of the Consolidated Fund of the government;

(b) securities the payment of which is guaranteed by the government, the government of Canada, the government of a province of Canada other than Manitoba, the government of a country other than Canada, or a financial institution;

(c) securities the payment of which is a charge on the Consolidated Revenue Fund of the government of Canada or a province of Canada;

(d) securities the payment of which is a charge on the revenue of a government of another country; and

(e) securities of a corporation authorized by or belonging to a class authorized by the Minister of Finance.

Appendix 9: Excerpt from the *City of Winnipeg Investment Policy*

Schedule 1

City of Winnipeg Short-Term Investments - Credit Risk Criteria

Investment Credit	DBRS	Moody's	S&P	Amount	Term
Government of Canada (minimum 10% of portfolio)					
Bonds	AAA	AAA	AAA	Unlimited	2 years or less
Treasury Bills	R1-High	P-1	A-1	Unlimited	1 year or less
Guarantees and Crown Corporations	R1-High	P-1	A-1	Unlimited	1 year or less
Provincial Governments and Guarantees (maximum 50% of portfolio)					
Bonds	AAA	AAA	AAA	$125 Million	2 years or less
	AA	AA	AA	$100 Million	2 years or less
	A	A	A	$50 Million	1 year or less
Treasury Bills,	R1-High	P-1	A-1	$125 Million	1 year or less
Promissory Notes, Guarantees	R1-Middle	P-1	A-1	$100 Million	1 year or less
	R1-Low	P-1/P-2	A-1/A-2	$50 Million	1 year or less
An individual credit shall not exceed (AAA R1-HIGH - $125M, AA R1-MID - $100M, A R1-LOW - $50M)					
Major Canadian Banks	R1-High	P-1	A-1	$100 Million	1 year or less
"Schedule I"	R1-Middle	P-1	A-1	$75 Million	6 months or less
(maximum 50% of portfolio)	R1-Low	P-1/P-2	A-1/A-2	$50 Million	3 months or less
An individual credit shall not exceed (AAA R1-HIGH - $100M, AA R1-MID - $75M, A R1-LOW - $50M)					
Schedule "II" Banks	R1-High	P-1	A-1	$50 Million	6 months or less
(maximum 25% of portfolio)	R1-Middle	P-1	A-1	$25 Million	3 months or less
An individual credit shall not exceed (AAA R1-HIGH - $50M, AA R1-MID - $25M)					

Note: An individual investment credit (except Government of Canada) shall not exceed 15% of the portfolio

City of Winnipeg Long-Term Investments - Credit Risk Criteria

Investment Credit	DBRS	Moody's	S&P	Amount	Term
Government of Canada and Guarantees (minimum 50% of portfolio)	AAA	AAA	AAA	Unlimited	Unlimited
	AA	AA	AA	Unlimited	Unlimited
Provincial Governments and Guarantees (maximum 50% of portfolio)	AAA	AAA	AAA	*1	30 years or less
	AA	AA	AA	*1	20 years or less
Municipalities	AAA	AAA	AAA	*2	30 years or less
(maximum 25% of portfolio)	AA	AA	AA	*2	10 years or less

Appendix 10: Summary of Audit Recommendations

As a result of the audit work, we are making nine recommendations that we believe, once implemented, will strengthen the administration of the City's reserves.

Recommendation 1
We recommend that the Chief Financial Officer conduct a review of the City's Investment Policy with respect to establishing performance objectives, benchmarks and reporting requirements. The results of the review should be communicated to Council with an appropriate recommendation for revisions.

Recommendation 2
We recommend that the Chief Financial Officer conduct a review of the City's investment strategy. The results of the review should be communicated to Council with a recommendation, if appropriate, to revise the current Investment Policy.

Recommendation 3
We recommend that as part of the City Treasurer's annual review of each reserve with the fund manager, an emphasis be placed on segregating the reserve's cash requirements into short-term, medium-term and long-term components. The recommended investment strategy should attempt to maximize the rates of return in the given market conditions through an appropriate mix of short and longer-term investments.

Recommendation 4
We recommend the Chief Financial Officer create an administrative directive, for approval by the CAO, to communicate the process and documentation standards required for the creation, amendment and ongoing administration of a reserve.

Recommendation 5
In conjunction with the development of a proposed policy on internal charges, we recommend that the CFO review the basis for the fees charged to reserve funds for management of the investment portfolio.

Recommendation 6
We recommend that the City Treasurer's Division report on the performance of the reserve funds annually to the fund managers and Council. The performance should be compared to portfolio targets that were mutually agreed with fund managers, based upon acceptable industry benchmarks.

Recommendation 7
We recommend that the Chief Financial Officer submit a report to Council, requesting an amendment to the Workers Compensation Reserve to reflect its current purpose as a fatality reserve. The report should also recommend repealing the existing by-law.

Recommendation 8
We recommend that the Cemeteries Administrator include in the business plan an evaluation of alternative business models for the cemeteries. In addition, and if applicable, the plan should include a detailed evaluation of the adequacy of the level of the reserve and a plan to ensure the reserve reaches an adequate funding level.

Recommendation 9
We recommend that the City Treasurer, as fund manager, revise the current administrative procedure such that the property taxes collected from the sale of City land be deposited in the General Revenue Fund.