

## CITY OF SALEM FINANCE DEPARTMENT

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Disability-related modification or accommodation, including auxiliary aids or services, in order to participate in this meeting or event, are available upon request. Sign language and interpreters for languages other than English are also available on request. To request such an accommodation or interpretation, contact the Finance Department at 503-588-6040 at least **two business days** before meeting; or TTD/TTY telephone (503) 588-6439, is also available 24/7.

### CITY OF SALEM AND SALEM URA FINANCE COMMITTEE

#### Committee Members

Councilor Tom Andersen, Chair  
Councilor Virginia Stapleton  
Councilor Trevor Phillips  
Councilor Jose Gonzalez  
Alternate-Councilor Jackie Leung

#### City Staff

Steve Powers, City Manager  
Dan Atchison, City Attorney  
Josh Eggleston, AIC Chief Financial Officer  
Jenny Mattechek, Chief Accountant  
Jeremy Morgan, Supervisor  
Anja Hill, Treasury Supervisor  
Kelli Blechschmidt, Management Analyst I  
Shengnan Thomas, Administrative Analyst I

#### Guest

Lauren Brant, PFM Managing Director  
David Reeser, CTP, EA, PFM Managing Director  
Allison Kaune, PFM Senior Analyst

Next Scheduled Meeting: December 20, 2021

It is the City of Salem's policy to assure that no person shall be discriminated against on the grounds of race, religion, color, sex, marital status, familial status, national origin, age, mental or physical disability, sexual orientation, gender identity, and source of income, as provided by Salem Revised Code 97. The City also fully complies with Title VI of the Civil Rights Act of 1964, and related statutes and regulations, in all programs and activities.

### MEETING AGENDA

#### Meeting Virtually

November 22, 2021

3:30 PM

View Via YouTube:

[https://www.youtube.com/channel/UCQLi9RKZNHu4wfYcs\\_TC0TA](https://www.youtube.com/channel/UCQLi9RKZNHu4wfYcs_TC0TA)

To sign up to testify via Zoom or to submit public comment, contact the Finance Department via email at [finance@cityofsalem.net](mailto:finance@cityofsalem.net) or telephone at 503-588-6040 by 1PM on November 22<sup>nd</sup>, 2021.

1. Call to Order
2. Approval of Minutes
  - a. October 25, 2021 (Package page 2)
3. Public Comment  
(Appearance of persons wishing to address the Committee on any matter other than those which appear on this Agenda.)
4. Action Items
5. Management Update/Information Items
  - a. ESG Investment Strategy Update (Package page 4)
6. Continued Business
7. New Business
8. Adjournment

# Finance Committee of the Salem City Council and the Urban Renewal Agency of the City of Salem Minutes

**DATE:** October 25, 2021

**CHAIRPERSON:** Tom Andersen

**PLACE:** Zoom

**STAFF LIAISON:**

Josh Eggleston

503-588-6130

[JEggleston@cityofsalem.net](mailto:JEggleston@cityofsalem.net)

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**Members Present:**

Chair Andersen  
Councilor Stapleton  
Councilor Phillips  
Councilor Gonzalez

**Members Absent:**

Alternate-Councilor Leung

**Staff Present:**

Dan Atchison, City Attorney  
Josh Eggleston, AIC Chief Financial Officer  
Jenny Mattecheck, Chief Accountant  
Anja Hill, Treasury Supervisor  
Kelli Blechschmidt, Management Analyst I  
Shengnan Thomas, Administrative Analyst I

**Guest Present:**

Lauren Brant, PFM Managing Director  
David Reeser, CTP, EA, PFM Managing Director  
Allison Kaune, PFM Senior Analyst

1. CALL TO ORDER: 4:00 PM / Quorum

2. APPROVAL OF COMMITTEE MINUTES

a. August 30, 2021

Motion was moved by Member Stapleton, seconded by Member Phillips and carried by the following vote:

Aye: Unanimous  
Nay: None  
Abstentions: None

3. Management Update/Information Items

a. Policy C-7 Investment Review

b. PFM Presentation

PFM Company Introduction by Lauren Brent, PFM Managing Director

Market portfolio update as presentation by Allison Kaune, PFM Senior Analyst.

Questions or comments by: Chair Andersen

Environmental, Social and Governance (ESG) Investing & Consideration presentation by David Reeser, PFM Managing Director.

Questions or comments by: Chair Andersen, Member Stapleton, Member Phillips, and Josh Eggleston, AIC Chief Financial Officer

Responses by: Lauren Brant, PFM Managing Director

c. Quarterly Investment Report (FY 2021-22 1st quarter) was provided for Committee review.

4. New Business

Chief Accountant Mattecheck asked the committee if they would like to keep the next meeting on Nov. 22 during Thanksgiving week. The committee decided to schedule a two-hour meeting on Nov. 22 at 3:30 pm, or 3:00 pm if there is a work session or executive session scheduled that evening.

5. ADJOURNMENT: 5:03 PM

The next meeting is scheduled for Monday, November 22, 2021 at 3:00PM or 3:30PM.

**FOR COMMITTEE MEETING OF: November 22, 2021**  
**AGENDA ITEM NO.: 5a**

**TO:** Salem City Council and Salem Urban Renewal Agency Finance Committee

**THROUGH:** Josh Eggleston, AIC Chief Financial Officer

**FROM:** Jenny Mattecheck, Chief Accountant

**SUBJECT:** ESG Investment Strategy Update

**ISSUE:**

Review opportunity to integrate measurable non-financial environmental, social, and governance factors (ESG) into the investment decision making process, as defined by Council Policy C-7, by engaging in additional advisory services offered by the City's investment advisors, PFM Asset Management LLC (PFMAM).

**RECOMMENDATION:**

Information only.

**SUMMARY:**

During the July 2021 meeting, the Finance Committee inquired about the City's investment policy and specifically if there was any guidance on what companies in which the City invested. In the response to these inquiries, staff prepared a report which included a detailed review of the City's current investment policy (Council Policy C-7) and an overview of investment policies held by several other Oregon municipalities. The report was provided to the Finance Committee during the October 2021 meeting as an informational agenda item (attachment 1).

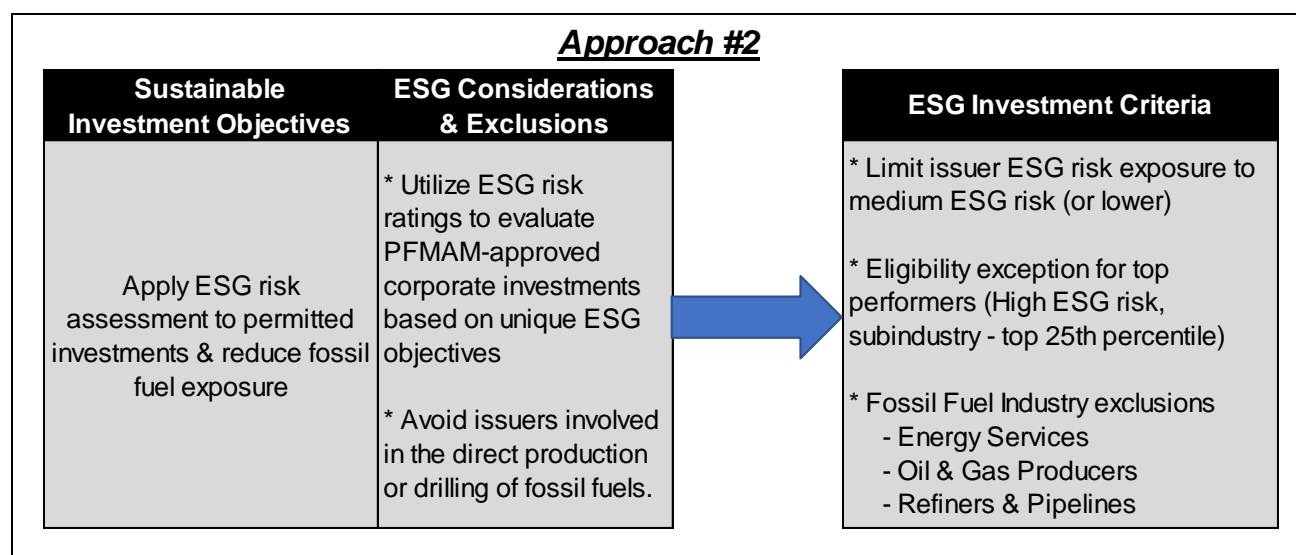
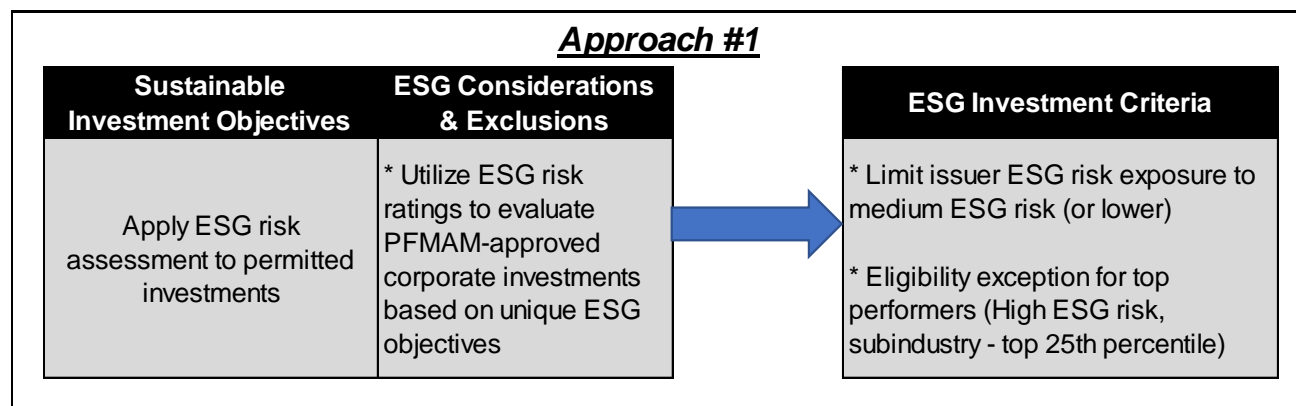
In addition to the staff report, PFMAM's Relationship Team presented an overview of the firm's Fixed Income ESG Investment Solution advisory service during the October 2021 meeting. At the conclusion of the meeting, the Finance Committee elected to extend the November 2021 meeting by an additional hour to allow for further review of PFMAM's ESG investing service offering and to discuss the City's potential engagement in these advisory services.

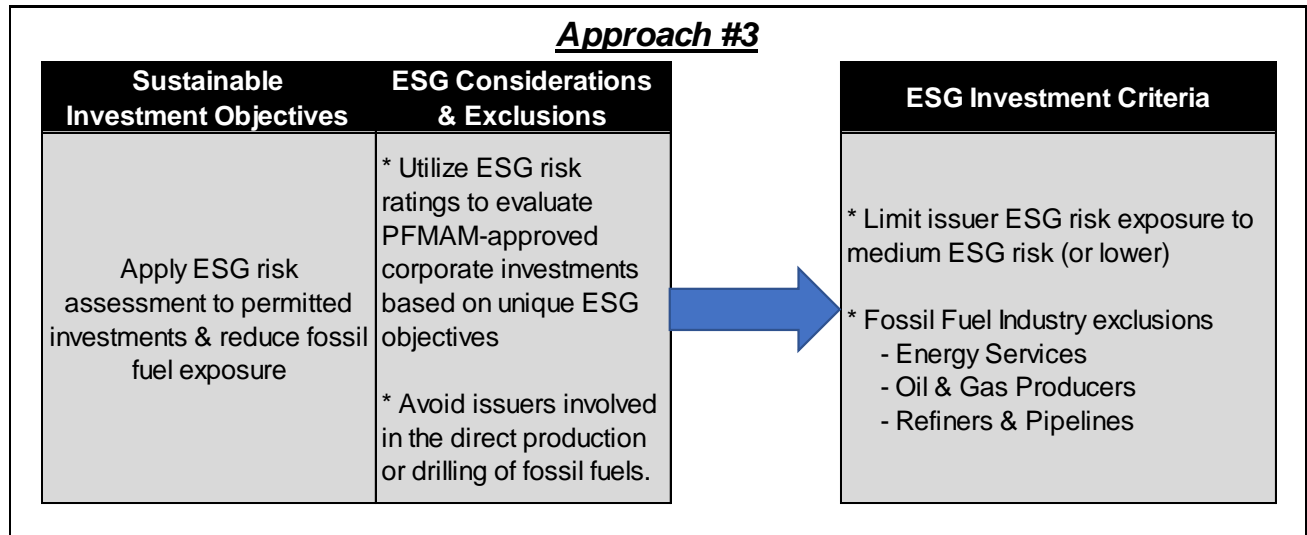
**FACTS AND FINDINGS:**

PFMAM has familiarity with local jurisdictions across the nation that have implemented an ESG factor review when making investments on behalf of the jurisdiction. After speaking with a jurisdiction about their ESG investment objectives, they will customize the portfolio and establish parameters for ESG investing. Companies to be considered appropriate for investment must meet the ORS requirements before they can be

considered within ESG investment parameters. PFMAM uses an ESG risk rating system which evaluates how companies limit their environmental impact, protect data, it's treatment of employees and more. Ongoing maintenance of the portfolio includes the consistent updating and review of these ESG factors, much like the current practice of monitoring a company's fiscal performance that currently takes place. The ESG approach employed by PFMAM also provides the City the with flexibility to efficiently adjust its ESG investment parameters if the City's sustainable investment objectives change.

Should the City engage with PFMAM in their ESG investing advisory services, the City would need to determine ESG investment objectives and parameters and incorporate any changes to Council Policy C-7. Three potential options for defining ESG investment objectives and parameters, which are common in practice, are shown below and concluded on the following page.





PFMAM's Relationship Team will attend the Finance Committee's November 2021 meeting and will provide further information on the mechanics of ESG investment strategies, explain how ESG scores are calculated including their assessment system, and provide an overview of the City's investment performance under the current investment strategy compared to the performance under a revised strategy in which ESG factors are incorporated. Additionally, PFMAM will provide an estimated increase to the advisory fee should the City elect to engage in the additional ESG investing advisory services.

## **BACKGROUND:**

The City's investment policy was last updated March 2018. Staff have identified recommended changes to the policy, such as the titles of officials. Staff will wait to provide these recommended changes until a conclusion is reached on whether to also revise the policy to include an ESG investment approach.

Should the Finance Committee recommend revising Council Policy C-7 for an ESG investment strategy, staff have identified the following as the required next-steps:

1. Finance Committee to provide approval of the final selections of the objectives and parameters for the ESG investing approach, including direction for implementation (i.e. allowing current investments not meeting revised policy to mature or sell those investments at the time the revised policy is adopted).
2. Staff, with the assistance of PFMAM, will revise Council Policy C-7 for the final ESG investment approach and forementioned recommended changes, such as titles of officials.
3. Approval of the revised Council Policy C-7 will be need from:

- a. Finance Committee
  - b. City Council
- 4. PFMAM will assist in the Oregon Short Term Fund (OSTF) Board review and approval process. Specifics regarding the review and approval process include the following:
  - a. Submission of revised policy and accompanying memo to the OSTF Board.
  - b. Submission of documentation to the OSTF Board is required by March 8, 2022 to be considered for review during the April 19, 2022 OSTF Board meeting.
- 5. Upon OSTF Board Approval, the City will execute an amended investment advisory agreement for the inclusion of the additional ESG strategy advisory services.
- 6. The City, with support of PFMAM's advisory team, will adopt and implement the revised Council Policy C-7.

#### Attachments

- 1. City of Salem - Council Policy C-7
- 2. Finance Committee Report – October 18, 2021

**COUNCIL POLICY NO. C-7**

**TITLE:** INVESTMENT POLICY AND PORTFOLIO GUIDELINES

**POLICY:** See attached.

**REFERENCE:** City Council Finance Committee Report dated 10/25/21, Agenda Item No. 5a  
(Supplants Amendment adopted 2/8/16 by Resolution No. 2016-6, Finance  
Division Staff Report 11/16/15 (Item 3(a))



**CITY OF SALEM INVESTMENT POLICY  
OCTOBER 2021**

I. Scope.....	3
II. Delegation of Authority .....	3
III. General Objectives.....	3
1. Safety.....	3
2. Liquidity.....	4
3. Yield.....	4
IV. Standards of Care; Ethics; Internal Controls .....	4
1. Prudence.....	4
2. Ethics and Conflicts of Interest.....	4
3. Internal Controls.....	5
V. Authorized Financial Institutions, Brokers-Dealers, Investment Advisers, and Depositories..	5
1. Authorized Financial Institutions and Brokers-Dealers.....	5
2. Investment Adviser.....	6
3. Delivery vs. Payment (DVP).....	6
4. Safekeeping.....	6
VI. Authorized Investments .....	6
1. Investment Types .....	7
2. Percentage of Investments, Maximum Maturity, and Credit Ratings by Type.....	8
3. Credit Ratings.....	9
VII. Investment Parameters.....	9
1. Diversification .....	9
2. Liquidity Requirements and Maturity Limits. ....	9
3. Bond Covenant Restrictions.....	9
4. Bids and Offers.....	10
5. Settlement Restrictions.....	10
6. Compliance Maintenance and Monitoring .....	10
VIII. Prohibited Investments .....	10
IX. Reporting and Performance Standards.....	10
1. Methods.....	10
2. Performance Standards.....	11
X. Policy Adoption and Re-adoption.....	11
Appendix I – Glossary .....	12
Appendix II: Authorized Finance Staff by Title .....	14

# CITY OF SALEM

## INVESTMENT POLICY AND PORTFOLIO GUIDELINES

The purpose of this Investment Policy (Policy) is to establish investment objectives, provide guidelines, and set forth responsibilities and reporting procedures necessary for the prudent management and investment of the funds of the City of Salem and its component units (the City). Financial terms can be found in **Appendix I –Glossary**.

### I. Scope

This Policy applies to the activities of the City of Salem with regard to the consolidated investment of short-term operating funds, reserves, and capital funds, including bond proceeds and bond reserve funds held by the City. Balances in checking accounts, negotiable order of withdrawal (NOW) accounts, investments of employees' retirement funds, and deferred compensation plans are not covered by this Policy.

### II. Delegation of Authority

The fiduciary responsibility and authority for the investment of City funds resides with the City Council. The City hereby designates the Financial Operations Manager as the Custodial Officer for the City's funds. The Custodial Officer shall be responsible for the operation of the investment program and shall act in accordance with ORS Chapter 294, Public Financial Administration, and written procedures and internal controls for the operation of the investment program that are consistent with this Policy. This Policy shall constitute a "written order" from the City Council per ORS 294.035.

The Custodial Officer, with the consent of the City Manager, may further delegate the authority to invest City funds to additional City Finance personnel listed in **Appendix II** of this Policy. No person may engage in an investment transaction except as provided under the terms of this Policy and procedures established by the Custodial Officer. The Custodial Officer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of delegees and other subordinate officials with access to the funds subject to this Policy.

### III. General Objectives

The investment objectives of this Policy and their priority are: (1) safety; (2) liquidity; and (3) yield.

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 in the overall portfolio. The objective shall be to remain compliant with applicable laws and to mitigate Credit Risk, Interest Rate Risk, and Custodial Risk.
  - a. **Legality.** All funds within the scope of this Policy are subject to regulations established by the State of Oregon; specifically ORS 294.035; 294.040; 294.052; 294.135; 294.145; and 294.810.
  - b. **Credit Risk.** The City will minimize the risk of loss by:
    - Limiting exposure to poor credits.
    - Pre-qualifying the financial institutions, Broker-Dealers, intermediaries, and advisers with which the City will do business.
    - Diversifying the investment portfolio so that potential losses on individual securities will be minimized.

- Actively monitoring the investment portfolio holdings for ratings changes, changing economic/market conditions, etc.
- c. **Interest Rate Risk.** The City will minimize the risk that the Market Value of securities in the portfolio will fall due to changes in general interest rates, by:
    - Structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities prior to maturity.
    - Investing the City's funds primarily in 0 to 5 year securities and overnight funds.
  - d. **Custodial Risk.** The City will minimize Custodial Risk by placing its securities with a third-party custodian, who will hold the securities in the City's name, as evidenced by the safekeeping contract and monthly statements.
2. **Liquidity.** The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by:
    - Maintaining appropriate balances in investment vehicles that provide overnight liquidity; and
    - Structuring the portfolio so that securities mature concurrent with cash needs to meet anticipated demands where possible and prudent.
  3. **Yield.** The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Securities shall not be sold prior to maturity with the following exceptions:
    - A security with declining credit may be sold early to minimize loss of principal.
    - A security trade will improve the quality, yield, or target duration in the portfolio.
    - Liquidity needs of the portfolio require that the security be sold.

#### IV. Standards of Care; Ethics; Internal Controls

1. **Prudence.** The standard of care to be used by the Custodial Officer and Custodial Officer's designees shall be the "prudent investor" standard and shall be applied in the context of managing all aspects of the portfolio.

The "prudent investor" standard requires investments to be made with judgment and care, under circumstances, then prevailing. The standard requires the exercise of reasonable care, skill and caution, and is to be applied to investments not in isolation but in the context of each investment fund's investment portfolio and as a part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the particular investment fund.

The Custodial Officer (Oregon Revised Statutes 294.004 (2)) and the Custodial Officer's designees acting in accordance with the prudent investor standard, this Policy, written policies and procedures ORS 294.035 and 294.040 and exercising due diligence, shall be relieved of personal responsibility for an individual security's Credit Risk or market price change or other loss in accordance with ORS 294.047, provided these deviations and losses are reported in a timely fashion and actions are taken to control adverse developments in accordance with this Policy.

2. **Ethics and Conflicts of Interest.** Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with the proper

execution and management of the investment program, or that could impair their ability to make impartial decisions. Employees and investment officials shall disclose in writing to the Custodial Officer any material interests in financial institutions that conduct business with the City. They shall further disclose in writing annually to the Custodial Officer any personal financial/investment positions that could be related to the performance of the investment portfolio. Employees, officers and their families shall refrain from undertaking personal investment transactions with the same individual with whom business is conducted on behalf of the City. Officers and employees shall, at all times, comply with ORS Chapter 244, Salem Revised Code, Chapter 12, and Human Resource Rule Section 8.2 (m).

3. **Internal Controls.** The Custodial Officer is responsible for establishing and maintaining an adequate internal control structure designed to reasonably protect the assets of the City from loss, theft, or misuse. The concept of "reasonable protection" recognizes that (1) the cost of control should not exceed the benefits likely to be derived and (2) the valuation of costs and benefits requires estimates and judgments by the Custodial Officer. Accordingly, the Custodial Officer shall establish a process for an annual independent review by an external auditor to assure compliance with this Policy and the internal controls established by the Custodial Officer. The internal controls should address the following points:

- Control of collusion
- Separation of transaction authority from accounting and record keeping
- Confirmation of transactions for investments and wire transfers
- Custodial safekeeping
- Avoidance of physical delivery of securities whenever possible
- Address control requirements for physical delivery where necessary
- Clear delegation of authority to subordinate staff members
- Development of a wire transfer agreement with the lead bank and third-party custodian and implementation of the appropriate safeguards
- Compliance and oversight with investment parameters including diversification and maximum maturities
- Staff training
- List of approved Brokers-Dealers, safekeeping and financial institutions

## **V. Authorized Financial Institutions, Brokers-Dealers, Investment Advisers, and Depositories**

1. **Authorized Financial Institutions and Brokers-Dealers.** The Custodial Officer shall maintain a list of financial institutions and brokers/dealers authorized to provide investment services. The list of approved financial institutions and brokers/dealers shall be selected through a process that ensures due diligence in the selection process. Financial institutions and brokers/dealers may include "primary" dealers or regional dealers that qualify under Securities and Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule). Regional brokers and dealers must have an office in Oregon in order to be considered for doing business with the City. The City will limit all security purchases to financial institutions and brokers/dealers on the approved list. Additions or deletions from the list shall be made at the Custodial Officer's discretion.

All financial institutions and Brokers-Dealers who desire to be considered for investment transactions, must supply the following, in writing (electronic delivery is acceptable):

- Audited financial statements
- Proof of Financial Industry Regulatory Authority, Inc (FINRA) registration

- Proof of state licensing
- Completed Broker-Dealer questionnaire
- Certification of having read and understood and agreeing to comply with the City's investment Policy
- Evidence of adequate insurance coverage

An annual review of the financial condition and registration of financial institutions and brokers/dealers on the list shall be conducted by the Custodial Officer.

If the City utilizes an external investment adviser, the adviser is authorized to transact with its own approved Broker-Dealer list on behalf of the City. The adviser will perform all due diligence for the Brokers-Dealers on its approved list. The adviser will annually provide the City their approved Broker-Dealer list so that the Custodial Officer may conduct its own review.

2. **Investment Adviser.** The Custodial Officer may engage the services of an external investment adviser to assist in the management of the City's investment portfolio. All investment transactions executed by the external investment adviser on behalf of the City must be consistent with this Policy and be pre-approved in writing by the Custodial Officer.

A list will be maintained of approved external investment advisers selected by the Custodial Officer using a fair selection process. An annual review of all external investment advisers shall be conducted by the Custodial Officer to determine their continued eligibility with the requirements below. All investment advisers shall:

- a. Be registered with the Securities and Exchange Commission (SEC) or licensed by the State of Oregon; (Note: Investment adviser firms with assets under management > \$100 million must be registered with the SEC, otherwise the firm must be licensed by the state of Oregon).
- b. Have certified that all of the representatives of the investment adviser who conduct investment transactions on behalf of this entity have read, understood and agreed to comply with this Policy.

If the City uses an external investment adviser, the adviser is authorized to enter into transactions with its own approved Broker-Dealer list on behalf of the City. The adviser shall perform all due diligence for all brokers/dealers on its approved list. The external investment adviser shall annually provide the City its approved Broker-Dealer list so that the Custodial Officer may conduct his or her own review.

3. **Delivery vs. Payment (DVP).** The Custodial Officer shall not pay for/deliver any securities until the Custodial Officer has received sufficient evidence of title/funding to the securities. Evidence of title must be consistent with modern investment, banking and commercial practices as specified in ORS 294.145 (4) and (5).
4. **Safekeeping.** Securities shall be held by an independent third-party safekeeping institution selected by the Custodial Officer. The Custodial Officer shall maintain a list of safekeeping institutions eligible to conduct business with the City. The safekeeping institution shall, upon request, provide a copy of its most recent Service Organization Control Report (SOC1 Report)

## VI. Authorized Investments

1. *Investment Types.* The following securities are permitted under this Policy as allowed by ORS 294.035 and 294.810. If additional types of securities become eligible for investment under Oregon law, investment in such securities shall not be permitted until this Policy has been amended.
  - a. **U.S. Treasury and Government Agency Obligations.** Lawfully issued general obligations of the United States, the agencies and instrumentalities of the United States or enterprises sponsored by the United States Government and obligations whose payment is guaranteed by the United States, the agencies and instrumentalities of the United States or enterprises sponsored by the United States Government.
  - b. **Oregon Short-Term Fund (OSTF)/Local Government Investment Pool (LGIP).** Oregon managed portfolio offered to governmental entities for the investment of public funds.
  - c. **Repurchase Agreements.** An agreement of one party to sell securities at a specified price to a second party and a simultaneous agreement of the first party to repurchase the securities at a specified price or at a specified later date. As provided in ORS 294.035(3)(j), only U.S. treasury obligations and government agency issues described in paragraph (a) of this subsection that are limited in maturity to three years and priced according to percentages prescribed by written Policy of the Oregon Investment Council or the Oregon Short-Term Fund Board may be used in conjunction with a Repurchase Agreement.
  - d. **Bankers' Acceptances.** A draft or bill of exchange drawn upon and accepted by a bank. Used as a short-term credit instrument, Bankers' Acceptances are traded at a Discount from face value as a money market instrument on the basis of the credit quality of the guaranteeing bank. Bankers acceptances must be: (i)Guaranteed by, and carried on the books of, a qualified financial institution; (ii)Eligible for discount by the Federal Reserve System; and (iii) Issued by a qualified financial institution whose short-term letter of credit rating is rated in the highest category by one or more nationally recognized statistical rating organizations.
  - e. **Corporate Indebtedness.** Commercial Paper and Medium Term Corporate Notes subject to a valid registration statement on file with the Securities and Exchange Commission or issued under the authority of section 3(a)(2) or 3(a)(3) of the Securities Act of 1933, as amended. Corporate indebtedness described in this paragraph does not include bankers acceptances. The corporate indebtedness must be issued by a commercial, industrial or utility business enterprise, or by or on behalf of a financial institution, including a holding company owning a majority interest in a qualified financial institution.
  - g. **Municipal Debt.**
    - i. Lawfully issued debt obligations of the agencies and instrumentalities of the State of Oregon and its political subdivisions that have a long-term rating of A-, or an equivalent rating or better, or are rated on the settlement date in the highest category for short-term municipal debt by a Nationally Recognized Statistical Rating Organization.
    - ii. Lawfully issued debt obligations of the States of California, Idaho and Washington and political subdivisions of those states if the obligations have a long-term rating of AA- or an equivalent rating or better or are rated on the settlement date in the highest category for short-term municipal debt by a Nationally Recognized Statistical Rating Organization.



Bonds described in this subsection may be purchased only if there has been no default in payment of either the principal of or the interest on the obligations of the issuing county, port, school district or city, for a period of five years next preceding the date of the investment.

**h. Time Deposit Accounts, Certificates of Deposit, and Deposit Accounts.**

- i. Deposits in insured institutions as defined in ORS 706.008, in credit unions as defined in ORS 723.006 or in federal credit unions, if the insured institution or credit union maintains a head office or a branch in Oregon.
- ii. Certificates of Deposit placed through deposit placement services, such as the Certificate of Deposit Account Registry Service (CDARS), are allowable so long as they comply with the requirements under ORS 295.004.

**2. Percentage of Investments, Maximum Maturity, and Credit Ratings by Type.**

Portfolio percentages shall be based on the Market Value of the investments at time of purchase. The maximum portfolio percentages for investments of surplus funds are as follows:

Security	Maximum % of Total Portfolio	Maximum Maturity	Credit Requirements
US Treasury Obligations	Up to 100 %	5 years	-
US Government Agency and Instrumentality Issues	Up to 100 % and 33 % per issuer	5 years	-
OSTF/LGIP	Statutory Limit (ORS 294.810)	-	-
Repurchase Agreements	Up to 10 % and 5 % per issuer	90 days	Collateral securing repo and margin requirements
Bankers' Acceptances	Up to 20 % and 10 % per issuer	6 months	A-1/P-1
Medium Term Corporate Notes*	Up to 35% and 5% per issuer	5 years	AA- or equivalent or better, or A or equivalent or better if the issuer meets the requirements of ORS 294.035(3)(i)(C)(i)(ii)
Commercial Paper		270 days	A-1/P-1 or better, or A-2/P-2 or better if the issuer is meets the requirements of ORS 294.035(3)(i)(C)(i)(ii)
Municipal Debt	Up to 10 % and 10% per issuer	5 years	Oregon: A- or equivalent or better, or A-1 or equivalent or better. CA, WA, ID: AA- or equivalent or better, or A-1 or equivalent or better
Time Deposit Accounts (CDs)	Up to 25 % and 10 % per issuer	2 years	Collateral requirements per ORS Chapter 295

Deposit Accounts	Up to 100%	-	Collateral requirements per ORS Chapter 295
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The maximum percent of Callable Securities in the portfolio shall be 25%.

Due to fluctuations in the aggregate surplus funds balance, maximum percentages for a particular investment type may be exceeded at a point in time subsequent to the purchase of a specific security. Securities need not be liquidated to realign the portfolio; however, consideration should be given to liquidation of that security when future liquidations are made.

3. **Credit Ratings.** Investments must have a rating from at least one Nationally Recognized Statistical Ratings Organizations, including, but not limited to, Moody's, Standard & Poor's, or Fitch Ratings Service.
  - a. The minimum weighted average credit rating of the portfolio's rated investments shall be in the categories of "Aa" by Moody's Investors Service; "AA" by Standard & Poor's; and "AA" by Fitch Ratings Service. Credit rating levels apply to the security on the transaction's settlement date.
  - b. If the credit rating of a security is subsequently downgraded below the minimum rating level for a new investment of that security, the Custodial Officer shall evaluate the downgrade on a case-by-case basis and determine whether the security should be held or sold. The Custodial Officer shall apply the general objectives of safety, liquidity, and yield in making such determination. That determination shall be documented in the quarterly report.
4. **Collateralization.** Cash management tools, defined as bank deposits, time deposits, Certificates of Deposit, and savings accounts, shall be held in qualified Oregon depositories which have met Oregon's Collateralization requirements per ORS Chapter 295. The Custodial Officer is responsible for the quarterly review of the State or Oregon's Approved Banking Institution list to ensure that banks in which such deposits and accounts are being held are on the approved list. The State of Oregon must be notified of changes in banking institutions.

## VII. Investment Parameters

1. **Diversification.** Investments shall be diversified by:
  - o Limiting investments to avoid over-concentration in securities from a specific issuer or business sector (excluding government securities).
  - o Limiting investment in securities that have high credit or interest risks.
  - o Investing in securities with varying maturities.
  - o Continuously investing a portion of the portfolio in readily available funds such as the OSTF/LGIP.
2. **Liquidity Requirements and Maturity Limits.** At all times, the City will maintain a minimum amount of funds to meet liquidity needs for the next three months. Unless matched to a specific cash flow requirement, the City shall not invest in securities maturing more than five years from the date of settlement. The Weighted Average Maturity of the City's portfolio shall at no time exceed 2.5 years.
3. **Bond Covenant Restrictions.** The investment of bond proceeds are restricted under bond covenants and tax laws that may be more limiting than this Policy. Bond proceeds shall be invested in accordance with the most restrictive parameters of this Policy and the applicable bond covenants and tax laws.



4. **Bids and Offers.** Each investment transaction shall be competitively transacted with financial institutions or Brokers-Dealers on the approved list. The Custodial Officer shall maintain a transaction record of each investment transaction. Competitive bids or offers should be obtained, when possible, from at least three financial institutions or Brokers-Dealers. In the event competitive bids or offers are not sought, the decision to do so shall be documented by the Custodial Officer. If the Custodial Officer uses an investment adviser, the investment adviser must retain documentation of competitive pricing execution on each transaction and provide such documentation to the Custodial Officer upon request.
5. **Settlement Restrictions.** Pursuant to ORS 294.145, the Custodial Officer is prohibited from making a commitment to invest funds or sell securities more than 14 business days prior to the anticipated date of settlement of the purchase or sale transaction.
6. **Compliance Maintenance and Monitoring.** Compliance with this Policy shall be maintained and be integral to each investment decision. Compliance status shall be reported to the Finance Committee at least quarterly, as described in Section IX. Out of compliance instances shall be reported to the Custodial Officer in a timely manner. The Custodial Officer shall determine the cure for non-compliance that is in the best interest of the City. Such action may include holding the investment to maturity, liquidating the investment, reversing the purchase, or adjusting future allowable investments until compliance is achieved.

## **VIII. Prohibited Investments**

Investment in the following securities is prohibited:

1. Private placement of "144A" securities. "144A" securities include Commercial Paper issued under Section 4(2)144A (also known as "4(2)A" of the Securities Act of 1933).
2. The City shall not lend securities nor directly participate in a securities lending program.
3. Reverse Repurchase Agreements.
4. Mortgage-backed securities.
5. Stock in any joint company, corporation or association.

## **IX. Reporting and Performance Standards**

1. **Methods.** Except where legally required to hold separate funds, the City will consolidate cash balances from all funds to maximize investment earnings. Net investment income will be allocated to the various funds at least quarterly based on their respective cash balances and in accordance with generally accepted accounting principles.

The Custodial Officer shall review a monthly investment management report that provides an analysis of the status of the current investment portfolio and transactions made over the last month. The report shall be provided to the Custodial Officer within a reasonable time after the previous reporting period end and shall include the following:

- List of transactions occurring during the reporting period
- List of individual securities held at the end of the reporting period, including security type, maturity date and call date
- Percentage of the total portfolio that each type of investment represents
- Weighted Average Maturity of the portfolio

The Custodial Officer shall provide a quarterly investment report to the Finance Committee, including a management summary that provides an analysis of the status of the current investment portfolio and transactions made over the last quarter. The report shall be provided within a reasonable time after the quarter end and shall include everything contained in the monthly report and the following:

- Status of compliance with this Policy
  - Book yield during the reporting period
  - Market value of portfolio holdings at the end of the reporting period
  - Performance of the portfolio relative to benchmark(s), as appropriate
2. **Performance Standards.** The investment portfolio shall be managed in accordance with this Policy. The Custodial Officer shall establish an appropriate benchmark or benchmarks, as appropriate, for investment parameters that reflects the types and maturities of investment allowed under this Policy. The Custodial Officer shall compare portfolio performance to the benchmark or benchmarks on a quarterly basis. It is anticipated the portfolio should attain a benchmark average rate of return over time. Factors influencing performance deviations shall be described by the Custodial Officer in the quarterly reports to the Finance Committee.

#### **X. Policy Adoption and Re-adoption**

1. This Policy may be reviewed by the vote of a majority of the Finance Committee. Changes shall be adopted by the City Council as amendments to this Policy. The data contained in the appendices to this Policy may be updated by the Custodial Officer as necessary, provided the changes in no way affect the substance or intent of this Policy.
2. OSTF Board review shall be requested for any material changes (e.g. changes in investment parameters, portfolio Duration, compliance issues, etc.) to this Policy.

## Appendix I – Glossary

**Bankers Acceptances:** A draft or bill of exchange drawn upon and accepted by a bank. Appropriate if guaranteed by, and carried on the books of, a qualified financial institution; eligible for Discount by the Federal Reserve System; and issued by a qualified financial institution whose short-term letter of credit rating is rated in the highest category by one or more Nationally Recognized Statistical Rating Organizations (NRSRO).

**Brokers-Dealers:** A bank or securities Broker-Dealer that is permitted to trade directly with the Federal Reserve System. Such firms are required to make bids or offers when the Federal Reserve System conducts open market operations, provide information to the Federal Reserve System's open market trading desk, and to participate actively in Treasury auctions.

**Bullet Notes/Bonds:** Notes or Bonds that have a single maturity date and are non-callable.

**Callable Securities:** A bond issue in which all or part of its outstanding principal amount may be redeemed before maturity by the issuer under specified conditions.

**Certificates of Deposits (CD):** A savings certificate entitling the bearer to receive interest. A CD bears a maturity date, a specified fixed interest rate and can be issued in any denomination. CDs are generally issued by commercial banks and are insured by the FDIC up to \$250,000. The term of a CD generally ranges from one month to five years.

**Certificate of Deposit Account Registry Service (CDARS):** A private service that breaks up large deposits (from individuals, companies, nonprofits, public funds, etc.) and places them across a network of banks and savings associations around the United States. Allows depositors to deal with a single bank that participates in CDARS but avoid having funds above the FDIC deposit insurance limits in any one bank.

**Collateralization:** Process by which a borrower pledges securities, property, or other deposits for the purpose of securing the repayment of a loan and/or security.

**Commercial Paper:** Short term unsecured promissory note issued by a company or financial institution. Issued at a Discount and matures for Par or face value. Usually a maximum maturity of 270 days, and given a short-term debt rating by one or more NRSROs.

**Coupon Rate:** Annual rate of interest received by an investor from the issuer of certain types of fixed-income securities. Also known as the "interest rate."

**Credit Risk:** Credit Risk is the risk that a security or a portfolio will lose some or all of its value due to a real or perceived change in the ability of the issuer to repay its debt.

**Custodial Officer:** The City has designated the Financial Operations Manager as the Custodial Officer for the City's funds.

**Custodial Risk:** Custodial Risk, or Custodial Credit Risk, is the risk of loss associated with the counter-party's (any entity that obtained the investment on a public entity's behalf) failure.

**Discount:** The amount by which the Par Value of a security exceeds the price paid for the security.

**Duration:** A measure of the timing of the cash flows, such as the interest payments and the principal repayment, to be received from a given fixed-income security. The Duration of a security is a useful indicator of its price volatility for a given change in interest rates.

**Government-Sponsored Enterprise:** A privately owned entity subject to federal regulation and supervision that was created by the U.S. Congress to reduce the cost of capital for certain borrowing sectors of the economy such as students, farmers, and homeowners. GSEs carry the implicit backing of the U.S. Government, but they are not direct obligations of the U.S.

Government. For this reason, these securities typically offer a yield premium over Treasuries. Examples of GSEs include: Federal Home Loan Bank (FHLB), Federal Home Loan Mortgage Corporation ("Freddie Mac"), Federal Farm Credit Bank (FFCB), and Federal National Mortgage Association ("FNMA").

**Interest Rate Risk:** The risk associated with declines or rises in interest rates which cause an investment in a fixed-income security to increase or decrease in value.

**Liquidity Risk:** Liquidity Risk is the risk that an investment may not be easily marketable or redeemable.

**Local Government Investment Pool (LGIP):** The state or Local Government Investment Pool offered to public entities for the investment of public funds.

**Market Value:** Current market price of a security.

**Nationally Recognized Statistical Rating Organization (NRSRO):** A credit rating agency that issues credit ratings that the U.S. Securities and Exchange Commission (SEC) permits other financial firms to use for certain regulatory purposes. Designated NRSROs include, but are not limited to, Standard & Poor's, Fitch, and Moody's.

**Oregon Short-Term Fund (OSTF):** A Local Government Investment Pool organized pursuant to ORS 294.805 through 294.895. Participation in the pool will not exceed the maximum limit annually set by ORS 294.810.

**Par Value:** Face value, stated value or maturity value of a security.

**Repurchase Agreements:** An agreement whereby the Custodial Officer purchases securities from a financial institution or securities dealer subject to an agreement by the seller to repurchase the securities. The Repurchase Agreement must be in writing and executed in advance of the initial purchase of the securities that are the subject of the Repurchase Agreement.

**Secondary Market:** Markets for the purchase and sale of any previously issued financial instrument.

**Treasury Bills (T-Bills):** Short-term direct obligations of the United States Government issued with an original term of one year or less. Treasury Bills are sold at a Discount from face value and do not pay interest before maturity.

**Treasury Bonds (T-Bonds):** Long-term interest-bearing debt securities backed by the U.S. Government and issued with maturities of ten years and longer by the U.S. Department of the Treasury.

**Treasury Notes (T-Notes):** Intermediate interest-bearing debt securities backed by the U.S. Government and issued with maturities ranging from one to ten years by the U.S. Department of the Treasury.

**Weighted Average Maturity (WAM):** The average time it takes for securities in a portfolio to mature, weighted in proportion to the dollar amount that is invested in the portfolio.

**Yield to Maturity (YTM at Cost):** The percentage rate of return paid if the security is held to its maturity date at the original time of purchase. The calculation is based on the Coupon Rate, length of time to maturity and original price. It assumes that coupon interest paid over the life of the security is reinvested at the same rate. The Yield at Cost on a security remains the same while held as an investment.

## **Appendix II: Authorized Finance Staff by Title**

Financial Operations Manager

Deputy City Manager

Financial Reporting Manager

Treasury Supervisor

Accounting Supervisor

**FOR COMMITTEE MEETING OF: OCTOBER 25, 2021**  
**AGENDA ITEM NO.: 5a**

**TO:** Salem City Council and Salem Urban Renewal Agency Finance Committee

**FROM:** Josh Eggleston, AIC Chief Financial Officer

**SUBJECT:** Policy C-7 Investment Review

**ISSUE:**

Review of Council Policy C-7 to provide Finance Committee information on the City's financial investments.

**RECOMMENDATION:**

Information only.

**SUMMARY:**

During the July 2021 meeting, the Finance Committee inquired about the City's investment policy and specifically if there was any guidance on what companies in which the City invested. Staff has reviewed our current investment policy, has spoken with our investment advisor (PFM Asset Management LLC) and have reviewed the investment policies from several other Oregon municipalities.

**FACTS AND FINDINGS:**

*Limitations*

Oregon Revised Statutes (ORS) 294.035 limits how much of a local government's portfolio can be invested in corporate indebtedness (including corporate notes and commercial paper) to 35%. Further, local governments can only have 5 percent of this category invested into any one company. As of September 30, 2021, the City has 11.8 percent of its portfolio invested in short and medium-term corporate notes spread over 12 separate companies.

The City is also limited by state statute to invest in companies with a rating of at least P-1 or Aa3 by Moody's Investors Service, A-1 or AA- by S&P Global Ratings, or A-1 or AA- by Fitch Ratings, or an equivalent rating by any nationally recognized statistical rating organization. However, if "a business is headquartered in Oregon, employs more than 50% of its permanent workforce in Oregon or has 50% or more of their tangible assets" [ORS 294.035 (3) (h)] then the rating requirements can be slightly lowered. Depending on the investment type, (e.g. bonds) there are additional limitations at the Federal level through agencies such as Securities and Exchange Commission and legislation like the Securities Act of 1933.

ORS does not include requirements or restrictions based on an issuer's ethical or

environmental standards.

### *Comparable Cities*

Staff looked at the following Cities investment policies: Albany, Bend, Corvallis, Eugene, Medford and Portland. Staff analyzed these policies for: ethical standards for companies, climate impacts, and if the policy had any specification of companies a City could invest.

As a matter of fiscal responsibility, a city's basic objectives for investments are safety – protecting assets from loss, liquidity – ensuring funds are accessible for cash flow needs, and yield – maximizing investment return so long as the first two objectives are met. These objectives are a standard for a City to make the smartest and safest investment of public funds in order to continue providing the essential services on which the community depends. The investment policies of the evaluated cities all included some form of Salem's investment objectives of safety, liquidity and yield. Additionally, some Cities like Corvallis and Bend have objectives like legality and portfolio diversification respectively. The City of Salem policy also includes these elements, but they are categorized within the safety objective.

Of the cities reviewed, only Eugene and Portland have particular guidelines or companies in which they can or cannot invest beyond what is in state and federal law. The City of Eugene adopted a resolution in 2014 which does not allow direct investment in the top 200 fossil fuel companies. The City of Portland also limits the companies in which they can invest by listing companies in their investment policy from which their financial advisor and staff can choose to invest for commercial paper. It is not clear from reading the policy how or why these particular companies were selected. Some of the companies on this list includes: Apple, Colgate-Palmolive, Johnson & Johnson, Alphabet Inc. (Google), Microsoft, Nike and Procter & Gamble. In prior years, the list also included Merck, Coca-Cola Co., 3M, Eli Lilly and Toyota. For all the other cities, ethics are mentioned in their investment policies regarding employees and custodians of the funds, but there are no standards of ethics for companies in which a city invests.

### *Environmental, Social and Governance Factors (ESG)*

The City's investment advisor has familiarity with local jurisdictions across the nation that have implemented an Environmental, Social and Governance (ESG) factor review when making investments on behalf of the jurisdiction. After speaking with a jurisdiction about their ESG investment objectives, they will customize the portfolio and establish parameters for ESG investing. Companies to be considered appropriate for investment must meet the ORS requirements before they can be considered within ESG investment parameters. PFM uses an ESG risk rating system which evaluates for how companies limit their environmental impact, protect data, it's treatment of employees and more. Ongoing maintenance of the portfolio includes the consistent updating and review of these ESG factors, much like the current practice of monitoring a company's fiscal

performance that currently takes place.

There are two main methodologies for ESG investments: using the ESG risk rating system or the exclusion of particular industries or sub-industries.. By using the ESG risk rating system as described by PFM, investments would be more easily managed as companies shift in their ESG rating and provide flexibility for staff and our investment advisor to make advantageous and timely changes to the portfolio. The ESG risk rating system itself could be adjusted to provide more specificity without directly limiting the companies which the City can or cannot invest. PFM staff will be available to discuss the City's portfolio, ESG generally and risk rating during the Finance Committee's October 25, 2021 meeting.

### **BACKGROUND:**

The City's investment policy was last updated March, 2018. Staff will be returning with some recommended changes to the policy, such as the titles of officials, at a future date.

#### **Attachments**

1. City of Salem - Council Policy C-7
2. Fix Income ESG Investment Solution Sheet – provided by PFM





# City of Salem, Oregon

## ESG Investment Considerations

### Presented by:

**Lauren Brant** | *Managing Director*

**Allison Kaune** | *Senior Analyst*

**David Reeser, CFA, CTP, EA** | *Managing Director*

**November 22, 2021**

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PFM Asset Management  
LLC

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Suite 1600  
Portland, OR 97232

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503.837.8445  
pfm.com



## Where We Are



Introduction to ESG investing



**Assess the portfolio's ESG performance**



**Evaluate ESG investment parameters**



Incorporate ESG investment criteria into the  
Investment Policy Statement



Integrate ESG into the management of the City's  
investment portfolio

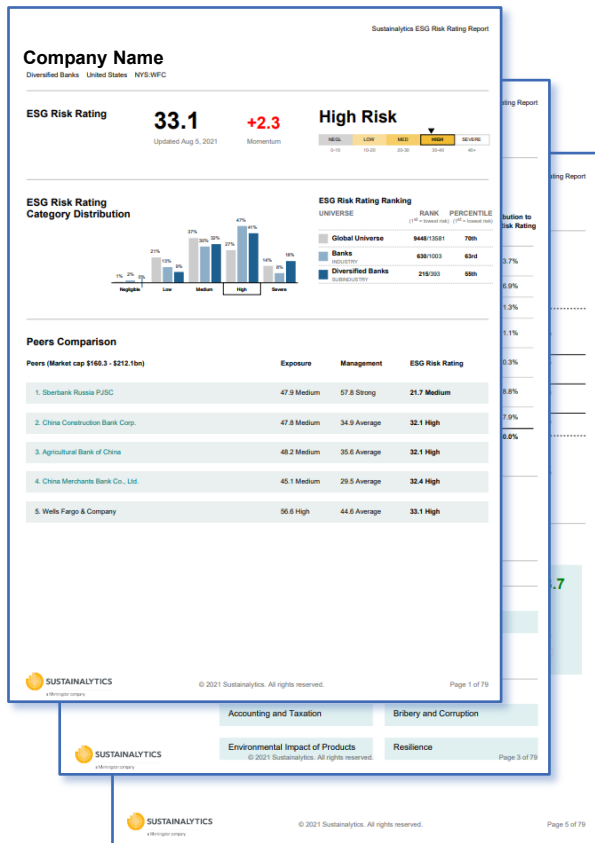


# Sustainalytics ESG Risk Rating Methodology





## Who Is Sustainalytics & What Is the ESG Risk Rating?

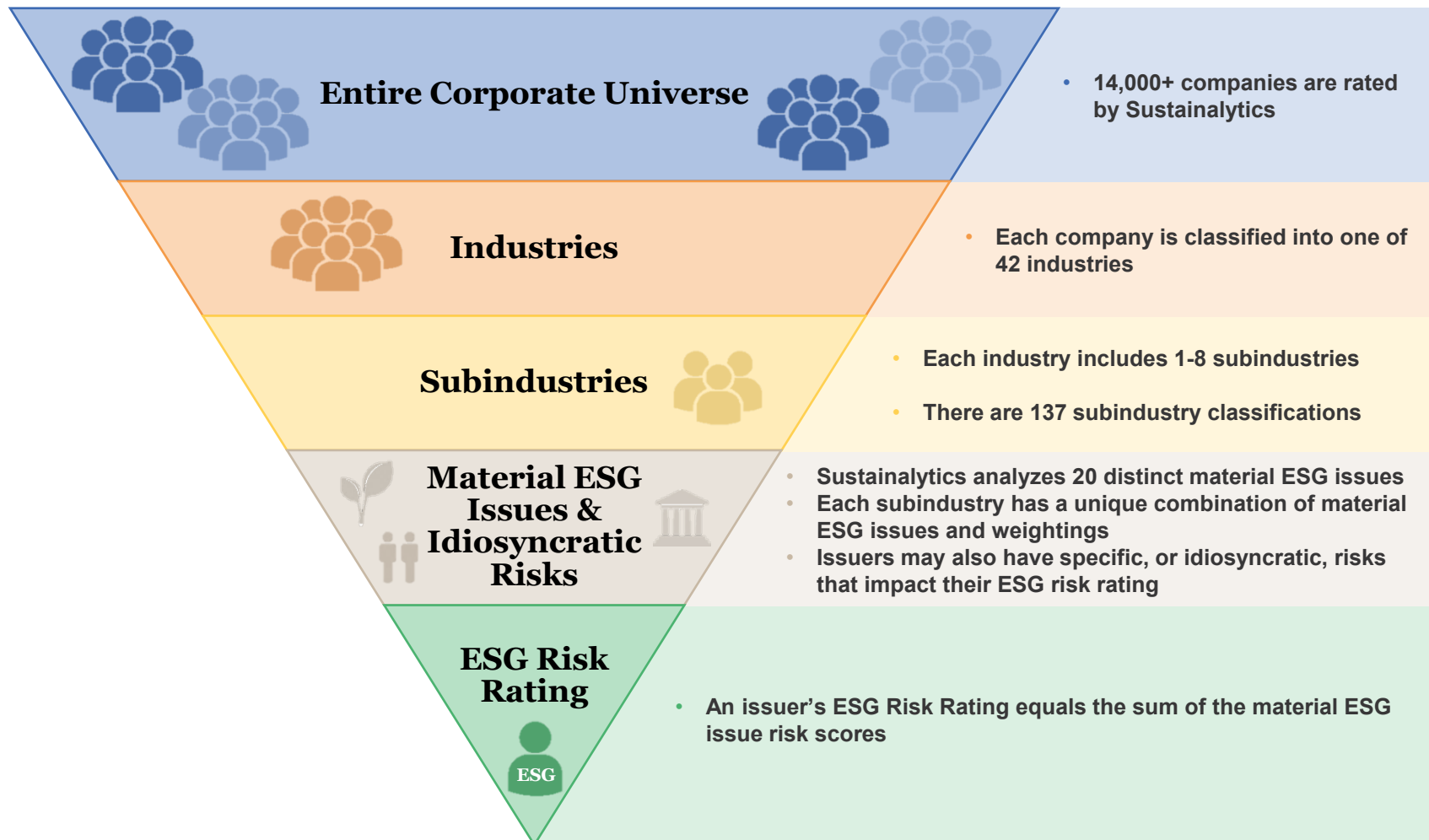


- A Morningstar subsidiary dedicated to independent ESG and corporate governance research, ratings, and analysis
  - Supports investors around the world with the development and implementation of responsible investment strategies, as it has done for over 25 years
  - Continuously conducts in-depth research and analysis on over 14,000 public and private companies
- Sustainalytics' **ESG Risk Ratings** enable investors to evaluate different organizations, using a consistent methodology, by quantitatively defining a company's material ESG risk on a scale of 0-100





## How Is ESG Risk Exposure Determined?





## Sustainalytics Industry Categories

- Sustainalytics has categorized each rated organization into 42 different industries and 137 subindustries
- ESG criteria may include an exclusionary component with exclusions based on specific industries and subindustries

Aerospace & Defense	Construction & Engineering	Electrical Equipment	Industrial Conglomerates	Precious Metals	Technology Hardware
Auto Components	Construction Materials	Energy Services	Insurance	Real Estate	Telecommunication Services
Automobiles	Consumer Durables	Food Products	Machinery	Refiners & Pipelines	Textiles & Apparel
Banks	Consumer Services	Food Retailers	Media	Retailing	Traders & Distributors
Building Products	Containers & Packaging	Healthcare	Oil & Gas Producers	Semiconductors	Transportation
Chemicals	Diversified Financials	Homebuilders	Paper & Forestry	Software & Services	Transportation Infrastructure
Commercial Services	Diversified Metals	Household Products	Pharmaceuticals	Steel	Utilities

Source: Sustainalytics





## Material ESG Issues



Material ESG Issue	Environmental	Social	Governance
Corporate Governance			✓
Access to Basic Services		✓	
Bribery and Corruption			✓
Business Ethics			✓
Community Relations		✓	
Data Privacy and Security		✓	
Emissions, Effluents and Waste	✓		
Carbon - Own Operations	✓		
Carbon - Products and Services	✓		
E&S Impact of Products and Services	✓	✓	
Human Rights		✓	
Human Rights - Supply Chain		✓	
Human Capital		✓	
Land Use and Biodiversity	✓		
Land Use and Biodiversity - Supply Chain	✓		
Occupational Health and Safety		✓	
ESG Integration – Financials*	✓	✓	✓
Product Governance		✓	✓
Resilience*		✓	
Resource Use	✓		
Resource Use - Supply Chain	✓		

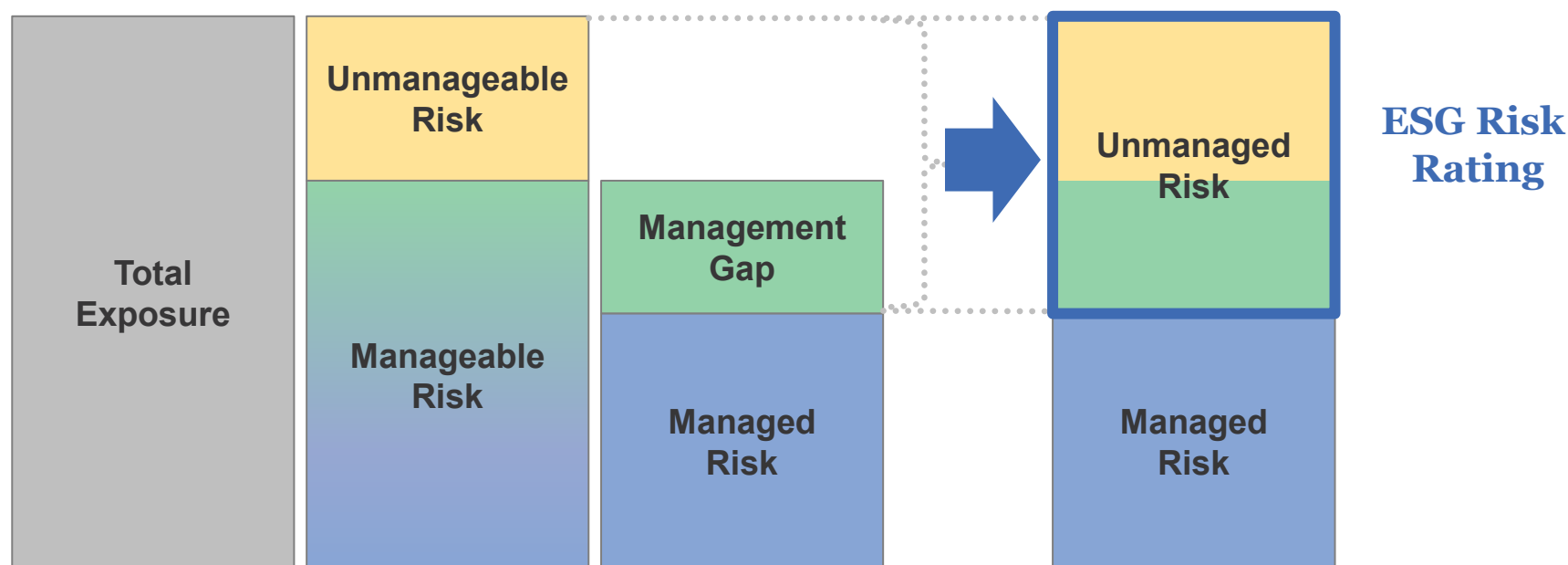
Source: Sustainalytics.

\* Only applies to financial companies.



## ESG Risk Rating Decomposition

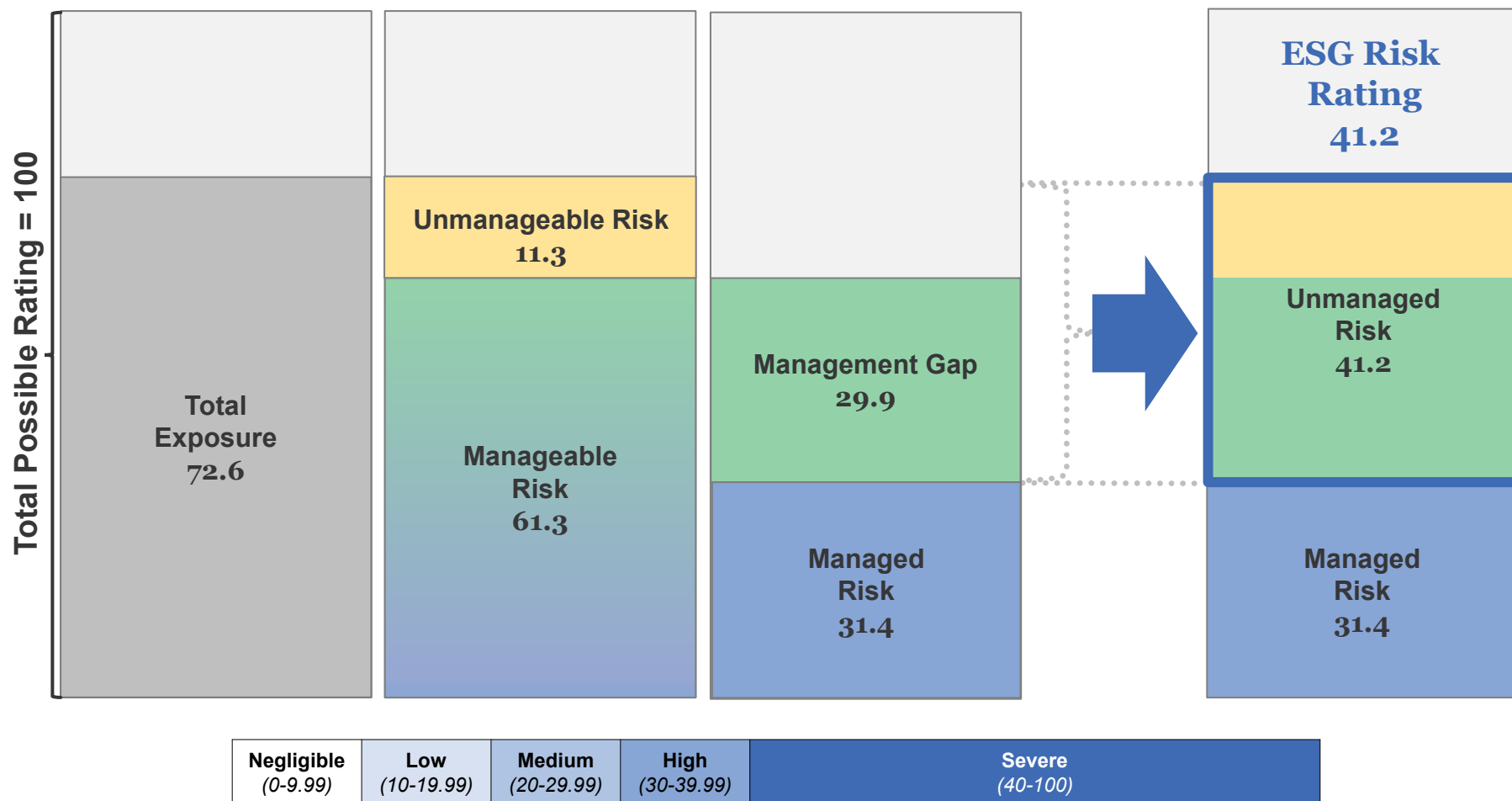
- ◆ **Total Exposure** is the starting point for a company's exposure to material ESG issues.
- ◆ Some companies have **Unmanageable Risks**, e.g., an oil company will always face risks related to carbon until it changes its business model.
- ◆ Of the **Manageable Risk**, a portion is managed through a company's policies, programs, management services, etc.; the remainder is considered unmanaged (**Management Gap**).
- ◆ The **ESG Risk Rating** evaluates unmanaged ESG risk.







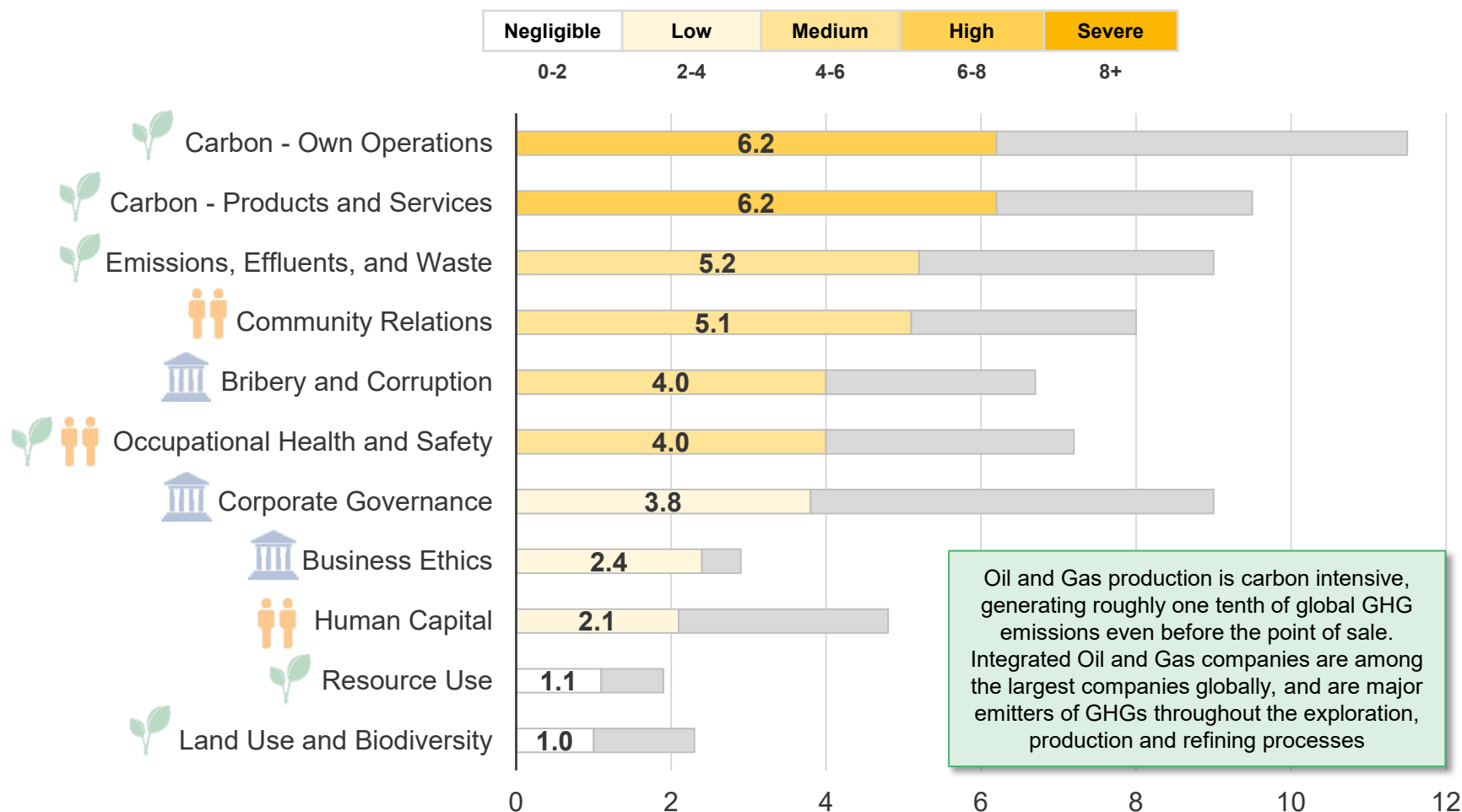
## ESG Risk Rating Example Calculation – Chevron Corp.





## ESG Risk Rating Decomposition Example Calculation – Chevron Corp.

■ Managed Risk Exposure ■ MEI Score / Contribution to ESG Risk Rating



Source: Sustainalytics. Last updated November 19, 2021.



# Investment Portfolio

## ESG Review & Analysis





## ESG Analysis Overview

### ◆ Summary of ESG Analysis

- The ESG-rated portion of the City of Salem's Long-Term Portfolio and Water-Sewer Rev Bond 2020 Portfolio had **medium** ESG risk as of October 31, 2021.\*
- Issuer ESG risk ratings ranged from low to severe. 80% of issuers maintained negligible, low, or medium ESG risk.
- Management of ESG risks among rated issuers was, on average, relatively strong.

### ◆ Key Assumptions & Methodology

- The enclosed presentation and analysis has been prepared based on the City of Salem's PFMAM managed portfolios as of October 31, 2021. Please see important disclosures at the end of this presentation.
- The analysis is based on Sustainalytics ESG risk ratings & metrics as of October 31, 2021. ESG data and ESG metrics are subject to change.
- ESG metrics have been applied to corporate issuers with ESG risk ratings, Fannie Mae, the Federal Home Loan Mortgage Corporation, and the Federal Home Loan Bank.

\* Based on the City of Salem's portfolios as of October 31, 2021. Market Value includes accrued interest. Sustainalytics data is as of October 31, 2021, and is subject to change. Please see important disclosures at the end of this presentation.



## City of Salem Investment Portfolio as of October 31, 2021 ESG-Rated Portfolio Overview

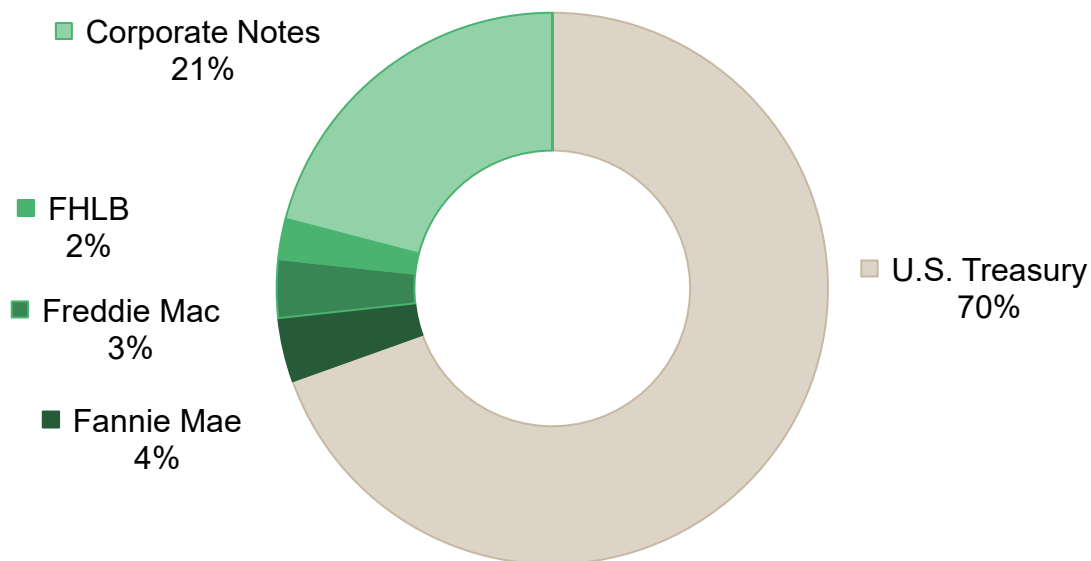
**15**/16 issuers with a MV of \$193.3 million<sup>1</sup>

**\$58,873,448 (30%)**

**Non-ESG Rated Issuers:**  
U.S. Treasuries

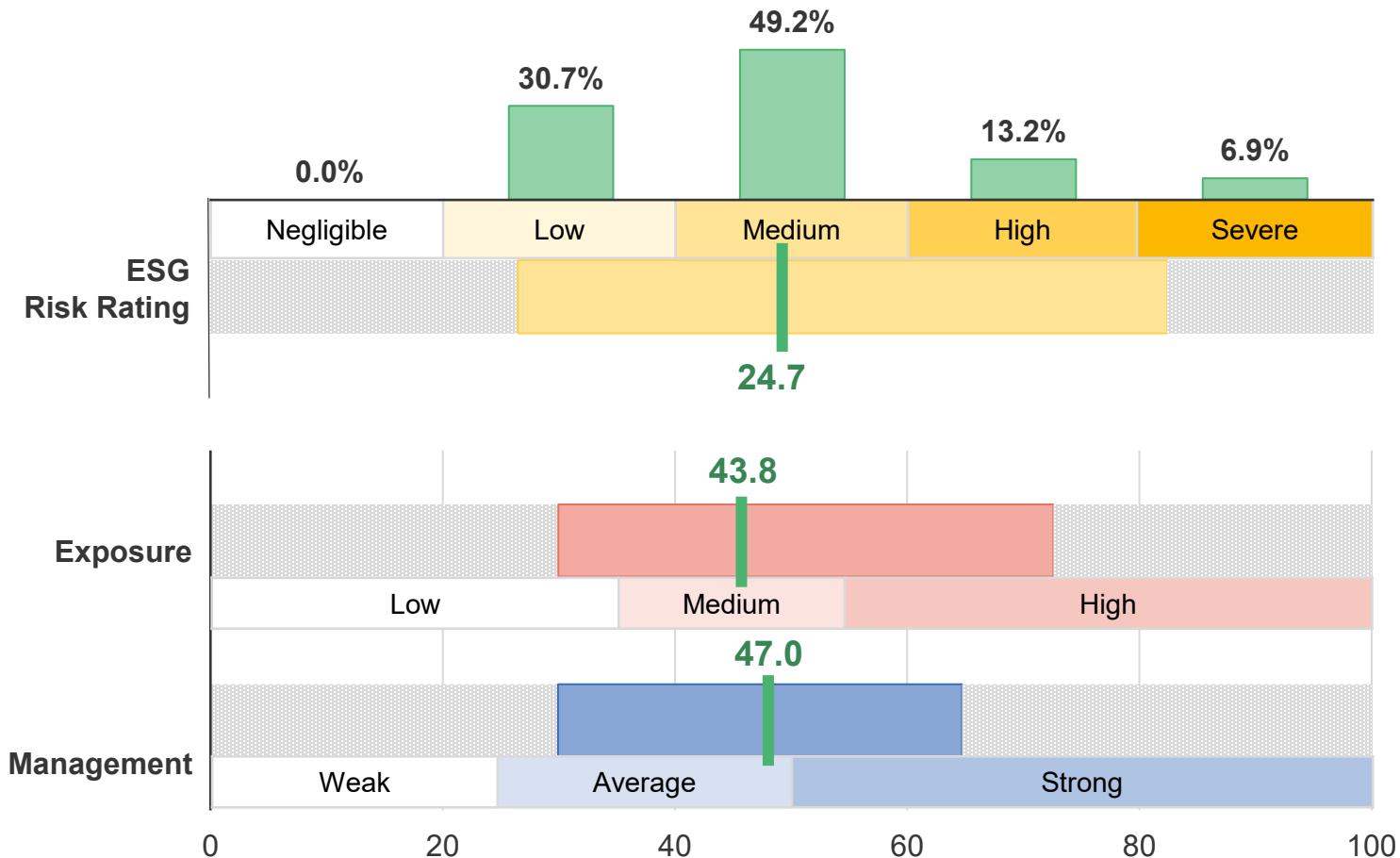
### Sector Allocation

*Green shades are ESG-rated sectors*





## City of Salem Investment Portfolio as of October 31, 2021 ESG Summary



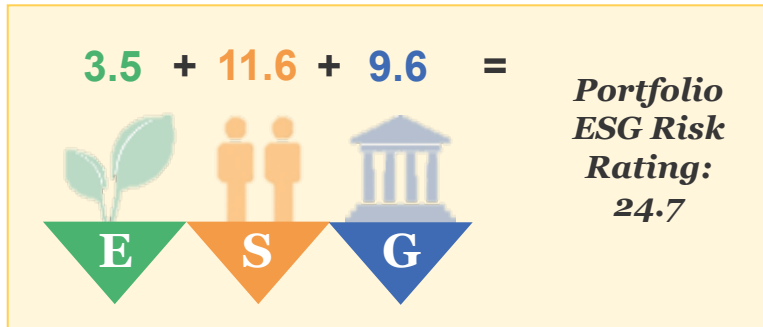
*Lower ESG Risk Ratings indicate better ESG risk profiles*

*Lower exposure scores generally result in lower ESG risk*

*Higher management scores generally reduce ESG risk*



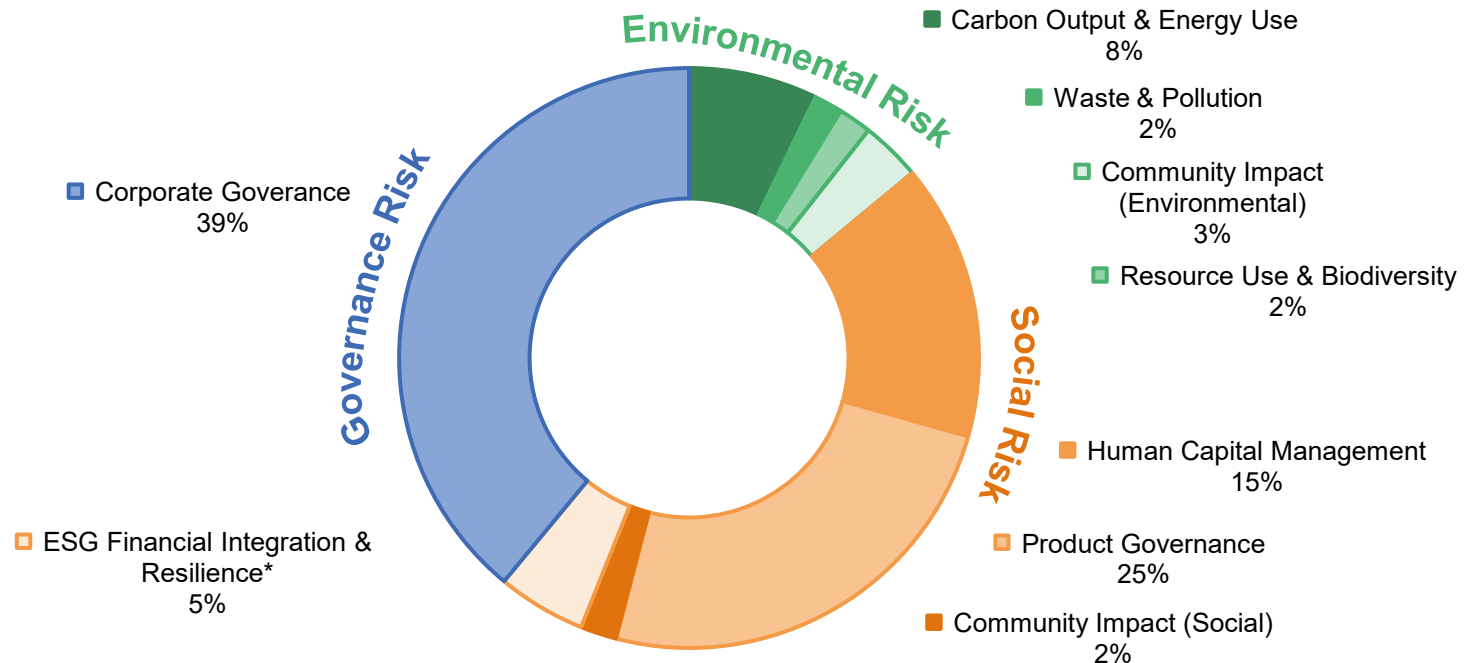
## City of Salem Investment Portfolio as of October 31, 2021 Risk Contribution by ESG Themes



*Environmental risk evaluates how a company manages its environmental impact and carbon footprint.*

*Social risk analyzes how a company treats employees, customers, the community, and other stakeholders as well as other companies it interacts with.*

*Governance risk assesses how a company is managed from the perspective of executive pay, internal controls, board composition, lobbying practices, and related issues.*



Source: Sustainalytics. ESG Themes were created by PFM based on the material ESG issues ("MEIs") and ESG indicators developed and defined by Sustainalytics. Please see the ESG Themes Glossary provided in the Appendix for additional information and details. \* Only applies to financial service industries.



## City of Salem Investment Portfolio as of October 31, 2021

### Issuer ESG Risk Ratings

Issuer	% Weight	Subindustry	Subindustry Percentile	ESG Risk Rating 10/31/21	Contributions		
					E	S	G
Microsoft Corp	1.1%	Enterprise and Infrastructure Software	3	13.3	6%	57%	37%
Visa, Inc.	0.3%	Data Processing	12	16.1	-	48%	52%
Apple Inc	4.2%	Technology Hardware	12	16.9	6%	39%	55%
Federal National Mortgage Association	3.7%	Thriffs and Mortgages	13	19.9	-	62%	38%
The Toronto-Dominion Bank	1.3%	Diversified Banks	12	20.3	6%	49%	45%
BlackRock, Inc.	1.1%	Asset Management and Custody Services	8	21.0	4%	45%	50%
Federal Home Loan Bank System	2.4%	Consumer Finance	24	23.7	-	56%	44%
Federal Home Loan Mortgage Corp	3.4%	Thriffs and Mortgages	30	24.8	7%	56%	37%
Procter & Gamble Co.	1.6%	Personal Products	27	27.0	37%	36%	27%
Bank of America Corporation	1.3%	Diversified Banks	32	27.0	5%	42%	53%
JPMorgan Chase & Co.	2.6%	Diversified Banks	36	28.0	3%	48%	49%
Johnson & Johnson	1.3%	Pharmaceuticals	8	29.0	3%	70%	27%
Amazon.com Inc	2.6%	Online and Direct Marketing Retail	91	30.0	23%	44%	33%
Toyota Motor Corporation	1.4%	Automobiles	57	30.4	22%	44%	34%
Chevron Corporation	2.1%	Integrated Oil & Gas	57	41.2	49%	26%	25%

Source: Sustainalytics data as of October 31, 2021. Portfolio holdings as of October 31, 2021. Issuers with “-” under ESG contributions means data not available.





# **ESG Investment Criteria Options**





## Proposed Sustainable Investment Objectives & ESG Approaches

### ● Potential ESG Considerations & Exclusions:

- Utilize ESG risk ratings to evaluate PFM-approved corporate investments based on unique ESG objectives
- Avoid issuers involved in the direct production or drilling of fossil fuels

#### **ESG Approach #1** *Overall Risk Rating + Top Performer Exception*

- Limit issuer ESG risk exposure to medium ESG risk (or lower)
- Eligibility exception for top performers (High ESG risk, subindustry – top 25<sup>th</sup> percentile)

#### **ESG Approach #2** *Overall Risk Rating + Top Performer Exception + Fossil Fuel Exclusions*

- Limit issuer ESG risk exposure to medium ESG risk (or lower)
- Eligibility exception for top performers (High ESG risk, subindustry – top 25<sup>th</sup> percentile)
- Fossil Fuel Industry exclusions:
  - Energy Services
  - Oil & Gas Producers
  - Refiners & Pipelines

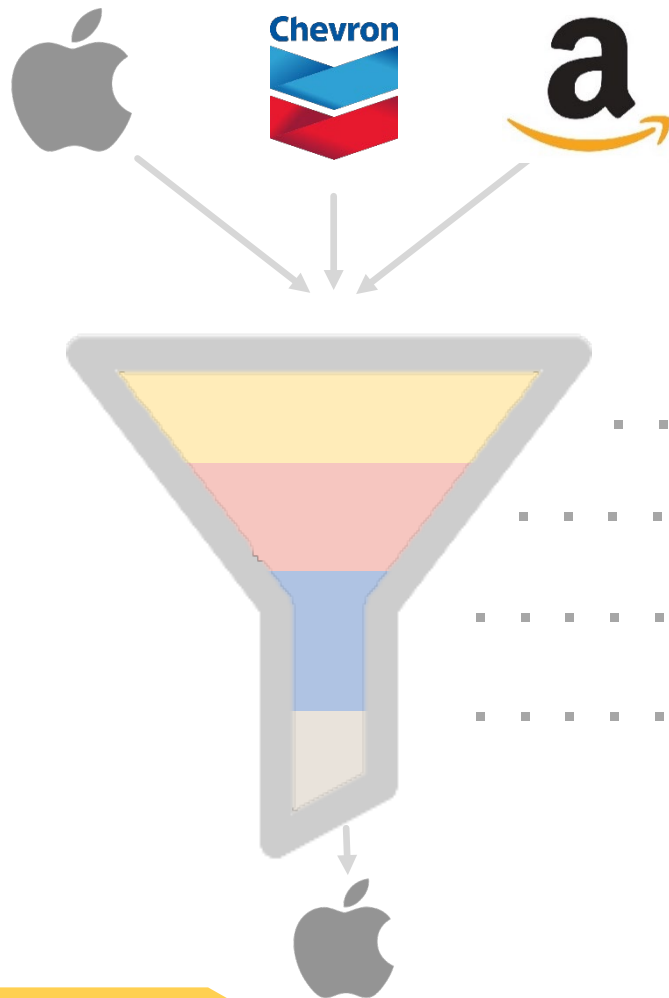
#### **ESG Approach #3** *Overall Risk Rating + Fossil Fuel Exclusions*

- Limit issuer ESG risk exposure to medium ESG risk (or lower)
- Fossil Fuel Industry exclusions:
  - Energy Services
  - Oil & Gas Producers
  - Refiners & Pipelines



## Example Application of ESG Investment Parameters

**ESG Approach #2**  
Overall Risk Rating +  
Top Performer Exception +  
Fossil Fuel Exclusions



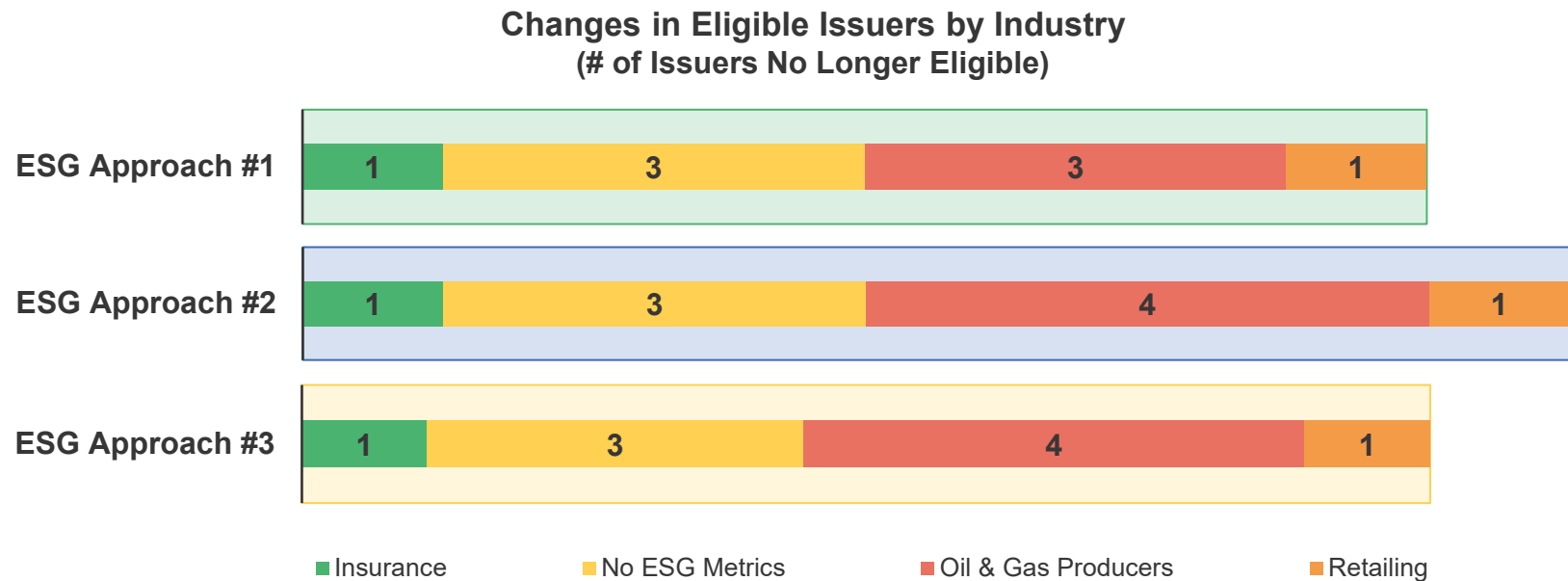
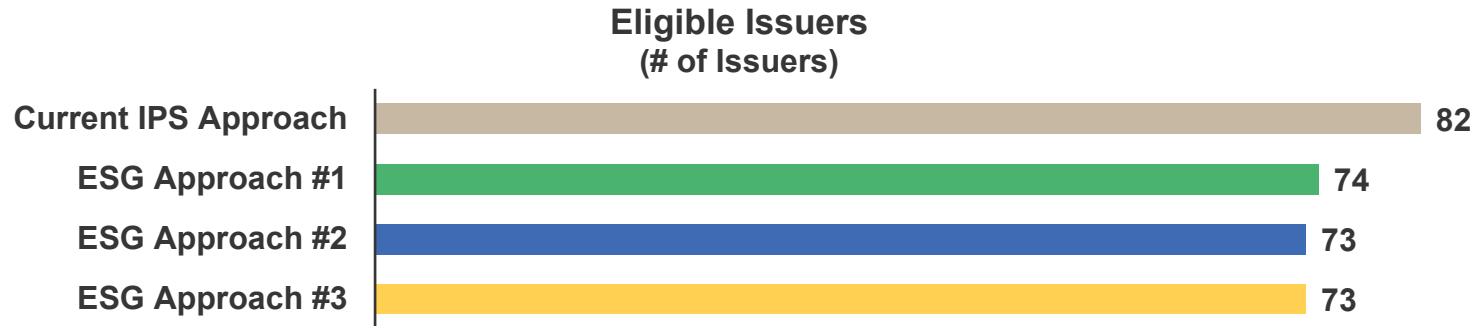
### Example ESG Investment Parameters

1. Maximum ESG Risk Rating medium or high if criteria #2 is met
2. Subindustry Rating Requirement = Top 25<sup>th</sup> Percentile  
(Rating  $\leq$  25<sup>th</sup>)
3. Industry Exclusions – Fossil Fuel industries

	Apple Inc	Chevron Corp	Amazon
Credit Ratings (S&P/Moody's/Fitch)	AA+ / Aa1 / - ✓	AA- / Aa2 / - ✓	AA / A1 / AA- ✓
ESG Risk Rating	Low ✓	Severe ✗	High ✗
Subindustry Ranking	12 <sup>th</sup> ✓	57 <sup>th</sup> ✗	91 <sup>st</sup> ✗
Industry	Technology Hardware ✓	Oil & Gas Producers ✗	Retailing ✓
Eligible Investment	YES	NO	NO



## Impact of Example Approaches on Eligible Corporate Issuers

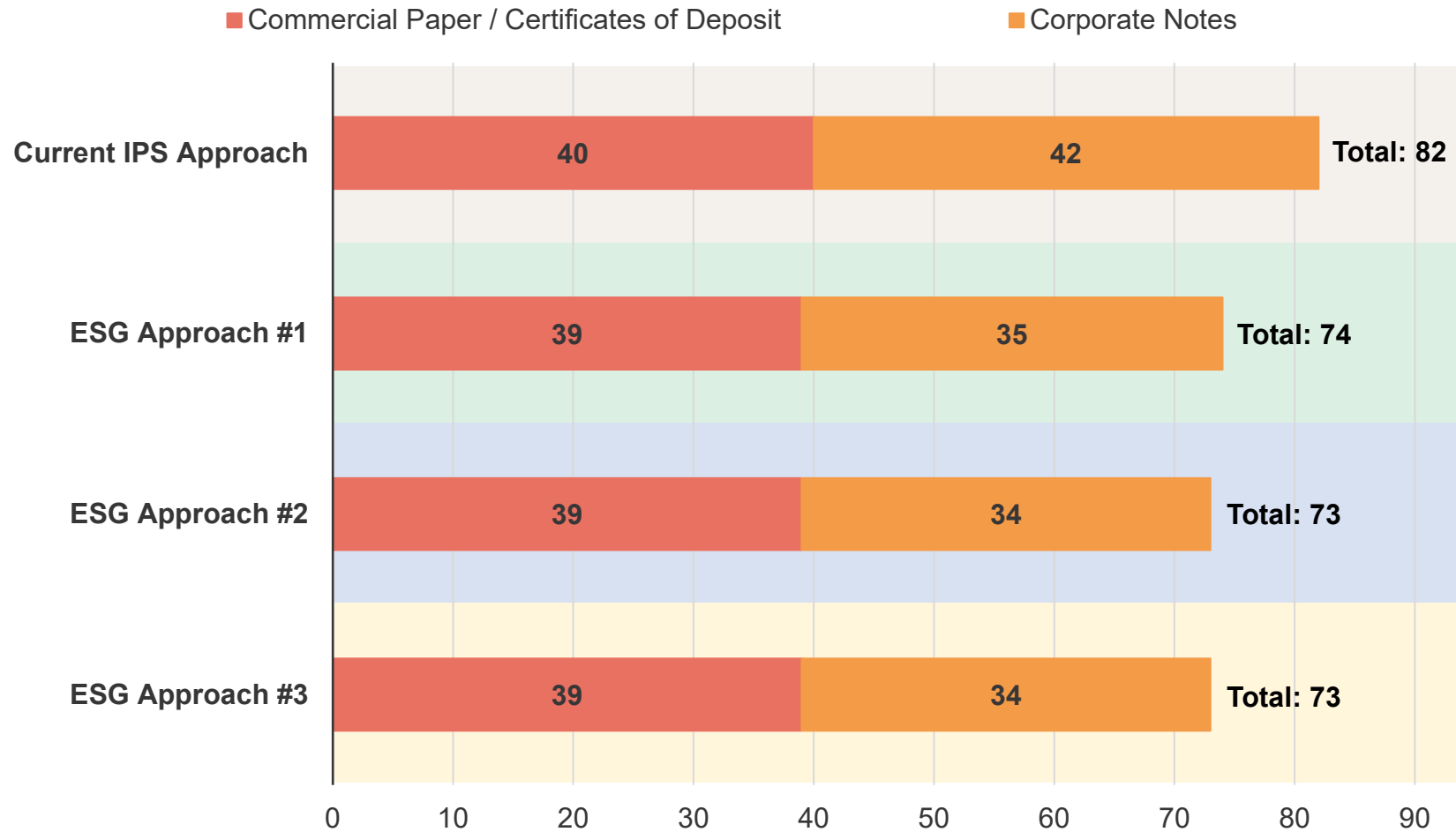


Based on PFMAM's Approved Issuer List as of 10/31/2021 and the City's Investment Policy Statement. Issuers without ESG risk ratings (No ESG Metrics) are not treated as eligible issuers in the sample ESG approaches.

\*Per the City's IPS, corporate issuers included are rated AA- or better by at least one NRSRO, and commercial paper must be rated A-1 or better by at least one NRSRO. Asset-backed securities are not permitted.



## Sector Diversification Impact on Approved Issuers



Based on PFMAM's Approved Issuer List as of 10/31/2021 and the City's Investment Policy Statement. Issuers without ESG risk ratings (No ESG Metrics) are not treated as eligible issuers in the sample ESG approaches.

\*Per the City's IPS, corporate issuers included are rated AA- or better by at least one NRSRO, and commercial paper must be rated A-1 or better by at least one NRSRO. Asset-backed securities are not permitted.



## Evaluating & Comparing Direct Costs and Potential Opportunity Costs

Direct Costs & Opportunity Costs	Additional Costs & Potential Impact
<i>PFMAM Fee Impact</i> →	<ul style="list-style-type: none"><li>• Additional fees would apply to assets managed in an ESG strategy and are 1 additional basis point (+0.01%) on total Portfolio AUM</li></ul>
<i>Custody &amp; Trading Costs</i> →	<ul style="list-style-type: none"><li>• Not applicable – Change in approach would <b>not</b> change custody fees or significantly impact trading activity</li></ul>
<i>Diversification Opportunities</i> →	<ul style="list-style-type: none"><li>• Reduction in approved issuers</li><li>• Remaining approved issuers provide diversification opportunities</li></ul>
<i>Yield &amp; Investment Return Impact</i> →	<ul style="list-style-type: none"><li>• Undetermined. Dependent on a number of factors, including:<ul style="list-style-type: none"><li>• Portfolio composition</li><li>• Liquidity</li><li>• Credit quality</li><li>• Change in yield spreads</li><li>• Direction of interest rates</li></ul></li></ul>



## PFMAM Fee Impact: \$200 Million Portfolio Total Annual Fee

Current PFMAM Fees			
Tier	Asset Value	Fee (bps)	Annual Fee (\$)
1	first \$ 50,000,000	9	\$ 45,000.00
2	next \$ 50,000,000	7	\$ 35,000.00
3	over \$ 100,000,000	6	\$ 60,000.00
<b>Total</b>		<b>7.00</b>	<b>\$ 140,000.00</b>

ESG PFMAM ESG Fees – Additional 1 bp (+0.01%)			
Tier	Asset Value	Fee (bps)	Annual Fee (\$)
1	first \$ 50,000,000	10	\$ 50,000.00
2	next \$ 50,000,000	8	\$ 40,000.00
3	over \$ 100,000,000	7	\$ 70,000.00
<b>Total</b>		<b>8.00</b>	<b>\$ 160,000.00</b>



## Next Steps for the City



**Determine ESG investment objectives & parameters and incorporate any changes to the Investment Policy Statement**



**Execute an amended investment advisory agreement**



**Identify ESG eligible permitted investments based on selected ESG investment parameters**



**Monitor the ESG risk ratings of the investments in the City's portfolio**



**Review, discuss, and refine the investment approach as needed**





# Appendix



# MEI Glossary



## ESG Themes Glossary

ESG Theme	Theme Description	Key Indicators
Environment	Carbon Output & Energy Use	<ul style="list-style-type: none"> <li>Carbon intensity</li> <li>Renewable energy use</li> <li>Env. Mgt. System certification</li> <li>GHG reporting / risk management</li> <li>Hazardous products</li> <li>Sustainable products &amp; services</li> </ul>
	Waste & Pollution	<ul style="list-style-type: none"> <li>Emergency response program</li> <li>Solid waste management</li> <li>Effluent management</li> <li>Radioactive waste management</li> <li>Hazardous waste management</li> <li>Non-GHG air emissions programs</li> <li>Oil spill disclosure &amp; performance</li> <li>Recycled material use</li> </ul>
	Resource Use & Biodiversity	<ul style="list-style-type: none"> <li>Biodiversity programs</li> <li>Deforestation programs / policies</li> <li>Site closure &amp; rehabilitation</li> <li>Water intensity &amp; risk management</li> <li>Forest certifications</li> <li>Supplier environmental programs / certifications</li> <li>Sustainable agriculture programs</li> </ul>
	Community Impact (Environmental)	<ul style="list-style-type: none"> <li>Env Impact – Community Relations</li> <li>Env Impact – Products &amp; Services</li> <li>Env Impact – Occupational Health and Safety</li> <li>Env Impact – Product Governance</li> </ul>

Source: Sustainalytics.



## ESG Themes Glossary

ESG Theme	Theme Description	Key Indicators
Social	Human Capital Management	<ul style="list-style-type: none"> <li>• Discrimination policy</li> <li>• Diversity programs</li> <li>• Gender pay equality / disclosures</li> <li>• Employee development</li> <li>• Supply chain management / standards</li> <li>• Human rights policies &amp; programs</li> <li>• Employee health &amp; safety</li> </ul>
	Product Governance	<ul style="list-style-type: none"> <li>• Product &amp; service safety programs / certifications</li> <li>• Data privacy management</li> <li>• Media &amp; advertising ethics policy</li> <li>• Organic products / GMO policy</li> <li>• Product health statement</li> </ul>
	Community Impact (Social)	<ul style="list-style-type: none"> <li>• Equitable pricing and availability</li> <li>• Access to health care</li> <li>• Price transparency</li> <li>• Human rights / indigenous policy</li> <li>• Community involvement programs</li> <li>• Noise management</li> </ul>
	ESG Financial Integration & Resilience*	<ul style="list-style-type: none"> <li>• Systemic risk management / reporting</li> <li>• Tier 1 capital</li> <li>• Leverage ratio</li> <li>• Responsible investment / asset management</li> <li>• Underwriting standards</li> <li>• Financial inclusion</li> <li>• Credit &amp; loan standards</li> <li>• Green buildings investments</li> </ul>

\* Only applies to financial service industries.  
Source: Sustainalytics.



## ESG Themes Glossary

ESG Theme	Theme Description	Key Indicators
<b>Governance</b>	Corporate Governance  Evaluates a company's rules, policies, and practices with a focus on how a company's board of directors manages and oversees the operations of a company. Also assesses the management of general professional ethics and lobbying activities	<ul style="list-style-type: none"><li>• Board/management quality &amp; integrity</li><li>• Board structure</li><li>• Ownership &amp; shareholder rights</li><li>• Remuneration</li><li>• Audit &amp; financial reporting</li><li>• Stakeholder governance</li><li>• Bribery &amp; corruption policies / programs</li><li>• Money laundering policy</li><li>• Whistleblower programs</li><li>• Business ethics programs</li><li>• Political involvement policy</li><li>• Lobbying and political expenses</li></ul>

Source: Sustainalytics.



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