

**CITY OF MANISTEE  
OIL AND GAS INVESTMENT BOARD  
MEETING OF AUGUST 15, 2014**

There will be a meeting of the Oil and Gas Investment Board held on Friday, August 15, 2014 at 12:00 p.m. in the Second Floor Conference Room, City Hall, 70 Maple Street, Manistee, Michigan 49660.

**AGENDA**

**I. ROLL CALL.**

**II. OLD BUSINESS.**

- a.) None

**III. NEW BUSINESS.**

- a.) Approval of Minutes from April 25, 2014
- b.) Bartlett Investment Update
- c.) Oil and Gas History
- d.) Oil and Gas Fund, Streets

**IV. COMMUNICATIONS.**

**V. PUBLIC COMMENT.**

**VI. ADJOURN.**

- c. Colleen Kenny, Chair  
Catherine Zaring, Council Representative  
Ed Bradford, Vice-Chair  
Doug Parkes  
Steve Brower  
Mitch Deisch, City Manager  
George Saylor, City Attorney  
Woody Uible, Investment Advisor

## OIL AND GAS INVESTMENT BOARD MINUTES OF APRIL 25, 2014

The City of Manistee Oil and Gas Investment Board held a regular meeting on Friday, April 25, 2014 at 12 p.m. in the Second Floor Conference Room, City Hall, 70 Maple Street, Manistee, Michigan 49660. Meeting was called to order by Chair Colleen Kenny.

**MEMBERS PRESENT:** Colleen Kenny, Doug Parkes, Ed Bradford, Steve Brower, Catherine Zaring

**MEMBERS ABSENT:** Mitch Deisch

**OTHERS PRESENT:** City Attorney George Saylor

### OLD BUSINESS

None.

### NEW BUSINESS

*Minutes* - Minutes from the January 17, 2014 meeting were reviewed. **MOTION** by Doug Parkes, second by Catherine Zaring to accept the minutes and place them on file. All in favor - motion carried.

*Amend Loan to Marina Fund* – The Oil and Gas Fund has an outstanding loan to the Municipal Marina in the amount of \$274,481.68 at 2% annual interest. The Marina has been unable to meet its obligations on this loan. The Board was asked to approve a change to the amortization schedule and authorize interest only payments in fiscal years 2013-2014 and 2014-2015. Board discussed the need to aggressively market the marina, the need to document this internal loan, and whether the interest rate was appropriate.

**MOTION** by Doug Parkes, second by Steve Brower, to authorize an interest only payment by the Municipal Marina for its outstanding loan from the Oil and Gas Fund in fiscal year 2013-2014 and 2014-2015; authorize updating the amortization schedule to reflect this; document this internal loan through a memorandum of understanding to be prepared by the City Attorney between the City and the Oil and Gas Board; and review interest rates again in five years. All in favor – motion carried.

*Investment Advisor Update and Commentary* – Woody Uible participated via phone to present the Investment Updates as of March 31, 2014. Information in the report includes Market Outlook, Comparison of Indices, Stock Earnings Yield Versus Bond Yield, Asset Allocation, Fixed Income Characteristics, Equity Sector Allocation, and Portfolio Performance. Questions

and comments by board members were responded to. First time this fund has gone over the 10 million dollar mark at the end of a quarter.

*Oil and Gas Spending Rule Sensitivity Analysis.* Finance Director Ed Bradford presented a Spending Rule Sensitivity Analysis that showed four hypothetical market situations and their impacts should this fund experience a significant downturn. This review shows that the smoothing effect of the twelve quarter moving average, the excellent portfolio performance over the last five years, and the reasonable spending percentage has set the City up for a relatively stable source of income for years to come. The one caveat noted was the analysis did not include tapping the excess earnings in the fund for other purposes as this would significantly impact the fund. Questions and comments by board members were responded to by the Finance Director and discussion included coverage of current obligations and legalities surrounding requests to use funds.

Chair Colleen Kenny left the meeting at 12:50 p.m., Vice-Chair Ed Bradford assumed the role of Chair.

#### **COMMUNICATIONS**

None.

#### **PUBLIC COMMENTS**

None.

#### **ADJOURNMENT / NEXT MEETING**

Next regular meeting is scheduled for Friday, July 25, 2014 at 12 p.m. in the Second Floor Conference Room, City Hall.

Motion to adjourn by Doug Parks, second by Steve Brower at 1:03 p.m.

Respectfully submitted,

*DRAFT* - cl

Cynthia Lokovich, CAP-OM  
Recording Secretary

- c. Manistee City Council  
Board Members  
Mitch Deisch, City Manager  
George Saylor, City Attorney



## Finance\Treasurer's Office



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**Memo to:** Mitch Deisch, City Manager

**From:** Edward Bradford, CFO *EB*

**Re:** Oil & Gas Fund History

**Date:** July 17, 2014

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Mitch,

In preparation for meetings of the Street Ad Hoc Committee and Headlee Override vote, I thought it would be useful to summarize important events and actions in the evolution of the Oil & Gas fund. The following table (Exhibit 1) presents information summarized from City Council minutes, Oil & Gas Board minutes and other archival data; however, it does not include every single event. I have highlighted what I believe to be important or noteworthy items.

After reviewing all of the information, I view the important points as follows:

1. Council has been consistent since the late 70's that the Oil & Gas principal (accumulated royalties and lease payments) be preserved for future generations.
2. The voters of Manistee ratified the Council(s) decision in November 1992 by approving a Charter amendment protecting the Oil & Gas principal. It passed overwhelmingly 82% to 18%.
3. City Council pledged earnings from the Oil & Gas fund as additional security for a water and sewer revenue bond issue in 1987. That pledge has been repeated in all subsequent revenue bond issues and is currently in effect.
4. The vast majority of Oil & Gas fund earnings have been transferred to the water and sewer fund. The total since 1984 is just over \$6,100,000 (Exhibit 2).
5. Council approved allocating any investment income over \$300,000 per year to the Street Improvement fund in 1988-1989 budget. This practice was discontinued in the 1999-2000 budget. Total amount allocated over this period appears to be  $\pm$  \$125,000.
6. Council approved establishing a capital improvement program in the 2005-2006 budget funded primarily by Oil & Gas investment earnings. Total transfers since establishment are just over \$2,400,000. (Exhibit 2)

7. State law was changed in 2008 to allow the Oil & Gas fund to be invested like a pension fund (PA 220 of 2008), vastly increasing the available investments, as well as increasing potential returns and risk.
8. Council adopted an Investment Policy and Spending rule, reviewed by the City Attorney, which calculates an annual spendable amount out of the Oil & Gas fund.
9. The Oil & Gas fund has been professionally managed by investment advisor Bartlett & Co. since 2009.
10. As of June 30, 2014 (unaudited), the Oil & Gas fund has a balance of \$10,409,776. Of this, \$7,388,977 is protected principal and the remainder is excess investment earnings.

A discussion of the current state of the Oil & Gas fund and different financial scenarios will be discussed in a second memo.

Exhibit 1		
Date	By	Action
12-6-1977	Council	Approved the seismic option and oil & gas lease option with Robinson & Cohen.
5-2-1978	Council	Non-drilling lease approved per option.
10-3-1978	Council	Approves surface location of wells with Aztec (Robinson & Cohen).
12-5-1978	Council	Received report of controlled well blowout.
5-15-1979	Council	Established escrow account for monies hoped to be received from oil & gas wells.
10-2-1979	Council	Received report from Aztec on wells. Described as "extremely prolific". Aztec proposes building a processing facility.
1-15-1980	Chamber of Com.	Requested Council use oil & gas money to build community center with pool and space for other activities and an area to seat 500 for dinner or meetings.
2-5-1980	Council	Aztec reviewed information on proposed sour gas sweetening facility.
2-18-1980	Council	Public hearing #1 on proposed sweetening facility.
2-19-1980	Council	Appointed committee to review plans and report back.
3-3-1980	Council	Public hearing #2 on proposed sweetening facility.
3-4-1980	Council	Aztec requests contract with City regarding operation of facility; study committee recommends construction if safeguards are in place; contract committee formed.
3-18-1980	Council	Aztec drafting contract for study committee review.
6-17-1980	Council	Discussion on methods to determine how to use oil revenues – no action.
4-1-1980	Council	Study committee recommended contract; Council approved contract for facility.
8-6-1980	Council	Resident informs Council of union picketing at plant construction site.
9-2-1980	Council	City Council voted to use oil & gas revenue for the #1 priority of storm & sewer separation.
1-6-1981	Manager	Lewis pointed out possibility of restricting oil money to investments and only using interest off those.

**Exhibit 1**

Date	By	Action
4-21-1981	Council	Directed attorney to draw up draft ordinance putting oil & gas funds in a trust fund and allow only using the interest.
5-20-1981	Council	Presentation and first reading of Oil & Gas Ordinance.
6-2-1981	Council	Second reading and Adoption of Oil & Gas Ordinance. Ordinance 40.
6-16-1981	Council	Appointed members to Oil & Gas Investment Board.
7-7-1981	Council	Approved amendments to oil & gas lease.
9-15-1981	Council	Approved oil & gas division orders.
12-15-1981	Council	Approved amendments to division orders.
6-15-1982	Council	Requested details of oil & gas investments.
7-20-1982	Council	Discussed extensive flooding due to combined sewers and 3.7" rainfall.
8-17-1982	Council	Council approved having an ongoing sewer construction project constantly in an effort to continue a program of sewer improvements and authorize use of oil & gas investment money or alternate funding.
5-17-1983	Council	Public hearing – resident requested royalties (around \$780,000) be spent on current operations. Mayor explained that interest is being used for sewer separation in Maxwelltown and the decision of Council was to conserve the principal as an investment to generate income now and in the future.
4-3-1984	Council	Approved additional oil & gas lease of City property to Aztec.
4-24-1984	Council	Work session with Aztec to discuss leases and production costs.
8-6-1984	Council	Established work session to review Aztec request to drill additional wells.
10-2-1984	Council	Approved drilling of two more wells east of Washington St.
1-3-1985	Manager	Lewis recommended using interest to fund WWTP activated sludge plant.
9-16-1986	Manager	Lewis explained the option of pledging oil & gas revenues for 15 years to help lower interest rate on WWTP bonds
10-15-1986	O&G	Minutes indicated O&G board was divided on how to best invest moving forward.
12-16-1986	Council	Fund at \$2,7891,000; Amend and ratify all existing oil & gas leases with Robinson\Cohen
12-16-1986	O&G	Authorized temporary transfer of funds to water & sewer fund until bond issue is completed; tabled bond issue escrow fund transfer request.
1-13-1987	O&G	Pledged revenues to the water and sewer fund with formal resolution to be adopted later; authorized additional \$300,000 of temporary transfer.
2-9-1987	O&G	Resolution to adopt bond ordinance 50.25 pledging all earned income to be paid to the water & sewer utility fund as additional security.
4-14-1987	O&G	Temporary transfers total \$709,000, additional \$130,000 needed, will be paid back when bond issue closes in May.
9-1-1987	Council	Discussed ordinance dedicating oil & gas revenue derived from ROW be used exclusively for ROW improvements, First reading of ordinance.
9-15-1987	Council	Adoption of Ordinance; adoption of resolution regarding investment goals; look at ways to audit oil & gas income. (This ordinance was never implemented.)
10-13-1987	O&G	Discussed City Council resolution requesting O&G retain a "qualified professional investment counselor"; need to generate more income to assist with WWTP.

**Exhibit 1**

<b>Date</b>	<b>By</b>	<b>Action</b>
11-10-1987	O&G	Special meeting to consider retaining an investment counselor.
12-3-1987	O&G	Board directs attorney to amend bylaws to allow engaging an investment advisor.
1-21-1988	O&G	Board amends bylaws and enters into agreement with Huber Fuger Wendin.
2-2-1988	Council	Authorized retention of Touche Ross to audit royalty income.
7/1/1988	88-89 Budget	Manager Bifoss proposes limiting interest income transferred to W&S to \$300,000 with remainder to go to street improvement fund.
10-11-1988	Council	Work session to discuss audit report.
5-1-1989	O&G	Manager Bifoss suggested item for future discussion about whether to make the oil & gas ordinance more secure for the future in case of Council changes.
7/1/81989	89-90 Budget	Manager Bifoss reinforced using income above \$300,000 to fund a multi-year accumulation of revenues for street work; alternate 5 mill not recommended at this time.
8-15-1989	Council	Council adopted resolution directing O&G to purchase DDA note.
8-22-1989	O&G	Approved \$60,000 promissory note to DDA for 10 years at 9%.
8-8-1990	Council	First reading of ordinance to remove bank president requirements from O&G board; instead two Mayor appointees.
8-23-1990	Council	Ordinance approved
5-7-1991	Council	Established work session on 5-14-91 with O&G Board to review investments.
12-17-1991	Council	Oil & Gas balance \$4,320,000
4-21-1992	Council	Approved resolution to place question of Charter restriction of oil & gas principal before the voters.
7-1-1992	92-93 Budget	Manager Bifoss proposed tapping street improvement fund to repair Maple Street Bridge over two-years.
8-18-1992	Council	Approved revised ballot language after Governor's review.
11-3-1992	Voters	Approved Charter amendment protecting Oil & Gas principal.
4-20-1993	Council	Approved revised investment policy for oil & gas fund.
3-21-1995	Council	Council adopted recodified ordinances, including Chapter 260 – Oil & Gas Investment Board, which replace Chapter 40.
7-1-1995	95-96 Budget	No excess earnings available for transfer to street improvement fund
12-19-1995	O&G	Annual City audit revealed investments not in compliance with State law, must be liquidated.
2-20-1996	O&G	Board terminated Heber Fuger and Wendin.
6-4-1996	Council	Approved revised investment policy for oil & gas fund.
7-1-1997	97-98 Budget	Minimal excess earnings again budgeted for transfer to street improvement fund
7-1-1999	99-00 Budget	No excess earnings <i>budgeted</i> for transfer to street improvement fund
7-1-2000	00-01 Budget	No excess earnings <i>budgeted</i> for transfer to street improvement fund

**Exhibit 1**

<b>Date</b>	<b>By</b>	<b>Action</b>
7-1-2001	01-02 Budget	No excess earnings <i>budgeted</i> for transfer to street improvement fund; appears prior policy has been discontinued.
7-3-2001	Council	Approved revised investment policy for oil & gas fund.
7-1-2005	05-06 Budget	Budget recommended funding capital improvement fund with oil & gas revenues and phasing out the water & sewer transfer over several years.
2-15-2006	O&G	New Aztec owners charging fees not in accordance with prior agreement; will contact and resolve.
1-16-2007	O&G	Discussed amending PA 20 to allow for greater investment flexibility.
4-17-207	O&G	Resolved to support pursuing change in State investment law.
5-1-2007	Council	Resolution supporting pursuing change in law impacting allowable investments for oil & gas fund.
10-24-2007	O&G	Finance director testified at Senate hearing on proposed law.
7-15-2008	O&G	SB 658 passed June 27, 2008 and was presented to Governor for signature. Public Act 220 of 2008.
9-4-2008	O&G	Recommended changes in Council Investment policy to Council.
10-7-2008	O&G	Approved revised City investment policy.
10-21-2008	O&G	Recommended Investment Policy and Spending Rule to Council.
11-18-2008	O&G	Sent out RFP for investment advisors.
12-2-2008	Council	Approved resolution granting investment authority to City chief investment officer; approved oil & gas investment policy and spending rule.
1-20-2009	O&G	Selected Bartlett & Co. as investment advisor.
8-06-2009	O&G	City attorney delivered opinion on spending rule and Charter; board recommended investment policy and spending rule amendments to Council.
8-18-2009	Council	Approved changes to gas investment policy and spending rule.
4-19-2011	O&G	Recommended changes to investment policy and spending rule.
2-07-2012	Council	Approved changes to investment policy and spending rule.
1-18-2013	O&G	Recommended changes to investment policy and spending rule, including lowering spendable amount and change to asset allocation.
3-19-2013	Council	Approved changes to oil & gas investment policy and spending rule.
4-19-2013	O&G	Approved interest bearing, internal loans from investment earnings to marina and boat launch; approved additional \$125,000 contribution to water and sewer fund.
4-25-2014	O&G	Approved amending loan to Marina by authorizing interest only payments for 2013-2014 and 2014-2015, and extending amortization schedule.

Exhibit 2

City of Manistee

Transfers to Water & Sewer Utility from Oil & Gas Fund

Year	Net Transfer	Transfer In	Transfer Out to Capital Improvement
1984	\$ 108,566		
1985	\$ 28,504		
1986	\$ 227,438		
1987	\$ 102,618		
1988	\$ -		
1989	\$ 209,577		
1990	\$ 281,436		
1991	\$ 321,361		
1992	\$ 348,265		
1993	\$ 345,292		
1994	\$ 247,192		
1995	\$ 274,169		
1996	\$ 299,305		
1997	\$ 347,636		
1998	\$ 331,173		
1999	\$ 301,415		
2000	\$ 323,272		
2001	\$ 332,905		
2002	\$ 321,472		
2003	\$ 283,668		
2004	\$ 246,804		
2005	\$ 217,151		
2006	\$ 182,779	\$ 224,779	\$ 42,000
2007	\$ 199,484	\$ 299,484	\$ 100,000
2008	\$ 157,069	\$ 332,069	\$ 175,000
2009	\$ -	\$ 200,000	\$ 200,000
2010	\$ -	\$ 200,000	\$ 200,000
2011	\$ -	\$ 320,770	\$ 320,770
2012	\$ -	\$ 342,782	\$ 342,782
2013	\$ -	\$ 365,548	\$ 365,548
2014	\$ 125,000	\$ 467,308	\$ 342,308
2015 Bud	\$ -	\$ 358,543	\$ 358,543
<b>Total</b>	<b>\$ 6,163,551</b>	<b>\$</b>	<b>\$ 2,446,951</b>



## Finance\Treasurer's Office



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**Memo to:** Mitch Deisch, City Manager

**From:** Edward Bradford, CFO *EB*

**Re:** Using \$3,000,000 from the Oil & Gas Fund

**Date:** July 18, 2014

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Mitch,

In 2008, after working diligently for over a year to amend state law to allow the City to invest its Oil & Gas Trust Fund (OGTF) in more appropriate manner, success was achieved. PA 220 of 2008 was signed into law in on June 27, 2008. The Oil & Gas Board (Board) in partnership with City Council then worked diligently to adopt an Investment Policy and Spending Rule (Policy) and select a qualified investment advisor in order to take advantage of the flexibility the new law provided.

Prior to the new law being passed, the OGTF had never been exposed to any significant amount of market risk, as the primary investments were local bank CD's, which have stable value. This investment approach was largely dictated by the previously mentioned limitations imposed by the State. As a result, for most of its existence, the OGTF was relatively simple to manage. Investments were made in CD's which generated interest earnings. As the CD's in the portfolio matured, they were reinvested in a laddered portfolio. Interest earned was transferred to the water & sewer fund as prescribed by ordinance. There were no realized or unrealized gains and/or losses to have to manage.

After the new law was passed, the City started investing the OGTF fund in the stock and bond markets in March of 2009 through its investment advisor, Bartlett & Co. March was the low point of the stock market after the financial meltdown of 2008. Six years later, the markets have yet to experience a significant downturn. Rather, the S&P 500 stock index has gone from 735 to 1,858, a 166% increase. This extraordinary bull market has allowed the OGTF to increase from approximately \$7,150,000 to \$10,400,000 today. In addition, it has provided almost \$2,300,000 in funding pursuant to the Policy over this time period.

The historical record makes it clear that markets do not go up indefinitely. Periods of growth are followed by periods of declines and subsequent recovery. Since implementing its new investment strategy, the OGTF has never experienced a market downturn. At the April 25, 2014 Board meeting, I presented an analysis of what the impact on the spendable amount would be under four hypothetical market situations. This analysis included input from our investment advisor as to plausible scenarios

and related returns. The scenarios reviewed were not intended to be all inclusive, but should cover about 80% to 90% of the types of events seen in the certain economic scenarios.

The takeaway is that the reasonable spending percentage, appropriate asset allocation, smoothing effect of the twelve quarter moving average (established in the Policy); and particularly the excellent portfolio performance over the last five years, have set up the community to enjoy a stable source of income for years to come.

Oil & Gas Trust Fund Scenarios						
Scenario	FY 2014 Spendable Actual	FY 2015 Spendable Actual	FY 2016 Spendable Projected	FY 2017 Spendable Projected	FY 2018 Spendable Projected	FY 2018 Spendable Projected
Average GDP Growth, moderate to good capital market returns	\$342,308	\$358,543	\$388,734	\$415,663	\$429,454	\$438,247
Below Average GDP Growth, sluggish capital market returns	\$342,308	\$358,543	\$386,132	\$406,703	\$412,463	\$414,154
Mod. recession, stock market decline, improved bond returns	\$342,308	\$358,543	\$374,856	\$377,194	\$366,383	\$364,041
Sharp recession, deep stock market decline, improved bond returns	\$342,308	\$358,543	\$361,469	\$348,365	\$322,667	\$318,814

However, one caveat in the analysis is that this assumes that there is not any action to tap the “excess investment earnings” in the fund for other purposes. The question was asked what the impact would be on using \$3,000,000 of OGTF money to immediately fund street repairs, instead of asking for a tax increase. This question can be answered, but requires key assumptions about things like future asset allocation, annualized rate of return, royalties received, investment horizon, spending rule percentage and the like. With that in mind, a simple analysis reveals the following if \$3,000,000 was tapped for street repairs:

- After 25 years, the OGTF would have \$4,837,000 less in value.

Ending Value of Oil & Gas Trust Fund after 25 Years	
No Withdrawal	\$16,155,000
Withdrawal of \$3,000,000	\$11,317,000
Difference	\$4,837,000

- The aggregate amount available under the spending rule would be less each year and the total amount available would be \$3,720,000 less.

<b>Reduction in Annual Spendable Amount</b>						
Year 1	Year 5	Year 10	Year 15	Year 20	Year 25	Total
\$40,000	\$132,000	\$145,000	\$158,000	\$174,000	\$190,000	\$3,720,000

- The risk of the OGTF becoming an “underwater endowment” (value less than the accumulated royalties) increases dramatically. In fact, I would say it is likely this would occur in the next market downturn. This would potentially require some significant changes in the way the OGTF is managed.



## Investment Policy & Spending Rule Oil and Gas Investment Board

Adopted: 8/6/09, Amended: 2/7/12

### I. Purpose

The purpose of this policy statement is to establish guidelines, policies and investment objectives for the City of Manistee's Oil & Gas Fund consistent with the directives of the City Council and applicable state law.

The purpose of the Oil & Gas Board is to manage and preserve the principal of the Oil & Gas Fund, while providing investment revenue to be used for the benefit of the citizens of the City.

### II. History of the Oil & Gas Fund

The City of Manistee receives royalties from oil and gas production on City-owned property and/or from City-owned mineral rights. This money is set aside in the Fund. The Fund principal is approximately \$6.7 million dollars as of June 30, 2008. The City Charter specifies that City Council shall not spend, loan or otherwise obligate any oil and gas royalty income or any of the principal in the Oil and Gas Fund without an affirmative vote by the majority of the electors of the City voting thereon.

The City of Manistee's Oil & Gas Fund and Investment Board (Board) was established in 1981 by City ordinance. This is codified as Chapter 260 in the Code of Ordinances. The stated purpose and intents of the ordinance is "...the preservation of the principal of oil, gas and related hydrocarbon revenues for the benefits of the citizens of the City." The Board is to "...manage, control, invest, re-invest and pay to the General Fund all income..." of the Fund.

Earnings from the Fund are currently sent to the Water & Sewer Utility Fund to subsidize the rates paid by the users of the system. This activity was authorized by a bond ordinance adopted when the City's large sewer separation project was being undertaken.

Council has chosen to gradually remove this subsidy through the annual budget process and transfer the earnings of the Fund to the Capital Improvement Fund. Water & sewer rates have been raised to offset this revenue loss to the water & sewer utility.

### III. Responsibility of the Board

The Board shall exercise oversight of the Fund consistent with Charter mandates, applicable statutes, Council directives, City ordinances and policies and this Investment Policy and Spending Rule document. The Board shall exercise prudence, judgment and due care when selecting investments and/or investment advisors (Advisor) and when reviewing the portfolio's performance.

#### **IV. Investment Objectives**

##### **Board Investment Philosophy**

The Board understands that a broad strategy of investing in a diversified portfolio of cash, stocks, bonds and real assets provides the best opportunity to attain the Fund's investment objectives. The Board seeks to achieve these objectives by investing in assets that over time will meet or exceed market returns as measured by relevant market and investment indices. The Board does not expect that all investment objectives will be attained in each year and recognizes that over various time periods, investments may produce significant over or underperformance relative to the broad markets. However, given that the Fund is perpetual and has a long time horizon, the strategy is designed to provide a satisfactory total return.

##### **Time Horizon**

It is intended that the investment objectives stated below will be achieved by the investment managers over a 5-year trailing period. However, the Board reserves the right to evaluate and make any necessary changes regarding the investment managers over a shorter-term basis using the criteria established in the "Selection of Investment Advisor(s)" section of this statement.

##### **Strategy and General Performance Objectives:**

The Fund is to be invested with the primary objectives of preserving the long-term real purchasing power of the Fund (net of inflation), and to provide a sustainable and stable level of income to support ongoing spending priorities. The objectives shall be accomplished by utilizing a balanced strategy of equities, fixed income and CD's held in local banks. Liquidity in the portfolio must be maintained to meet all reasonably anticipated spending requirements. Furthermore, the portfolio should consist largely of securities with active secondary markets. The portfolio will invest in equity or equity-like securities to provide adequate long term growth of capital. Fixed income securities will be used to lower the short-term volatility of the portfolio and to provide income stability, especially during periods of weak or negative equity markets. Cash is used as a strategic asset class for liquidity and spending needs. The portfolio will remain invested within the stated asset allocation ranges. The investment manager shall act within a reasonable period of time to correct deviations from these ranges.

#### **V. Available Investments**

Michigan State Law limits the types of investments that the Oil and Gas fund may participate in. It is governed by PA 220 of 2008 which is codified as Section 7 of PA 20 of 1943, being MCL 129.97. This section states that, Charter provisions notwithstanding, the Oil & Gas fund to be invested in the same fashion as an investment fiduciary may invest under the public employee retirement system investment act, 1965 PA 314, MCL 38.1132 to 38.1140m.

#### **VI. Allowed Investments \ Asset Allocation**

It is the Board's intention to not limit flexibility within the portfolio by specifying a rigid, narrow set of allowable investments. The broad limitations specified by 1965 PA 314, MCL 38.1132 to 38.1140m apply to Fund investments. This is consistent with the purpose of getting the legislature to pass PA 220 of 2008, so that the City could invest the Fund in

a more appropriate mix of investments that maximizes the benefits of having had the foresight to set aside the oil & gas royalties in perpetuity.

However, the Board has established general categories of asset classes. The broad classes of assets and allocations are shown in Appendix 1, which shall be updated by the Board from time to time.

Further, the Board has specifically identified assets which are allowed by law, but which the Fund *will not invest in*:

- Illiquid securities (non-exchange traded or those for which there is not a ready market);
- Short sales;
- Direct investment in futures or options on futures;
- Puts, calls, straddles or other option strategies;
- Purchase of real estate, with the exception of Real Estate Investment Trusts;
- Non-dollar denominated securities; and
- Non-exchange traded derivatives
- Debt Swaps
- Currency

The Board expects to invest, or shall direct the Advisor to invest, approximately 10% of the Principal with local banks. Local banks are defined as those that have an office anywhere in Manistee County.

#### **VII. Selection of Investment Advisor(s)**

The Board may select one or more investment advisors (Advisors) to manage the portfolio. The following criteria shall be considered when selecting an investment advisor:

1. Assets under management;
2. Experience, qualifications of personnel, financial resources and staffing levels;
3. Education and professional credentials;
4. Reference checks;
5. Experience with endowed funds;
6. Past performance, considered relative to other portfolios having similar investment objectives. Consideration shall be given to both consistency of performance and the level of risk taken to achieve results;
7. The investment style and discipline of the investment manager;
8. Quality of periodic financial reports and statements; and
9. Fee schedule

#### **VIII. Duties of Investment Advisor**

The Advisor is responsible for assisting the Board in all aspects of managing and overseeing the Fund's investment portfolio. The Advisor is the primary source of investment education and information. On an ongoing basis the Advisor will:

- Ensure compliance with this document and applicable law;
- Recommend the appropriate asset allocation policy and target ranges;
- Invest the Fund in a manner appropriate to meet the investment objectives;
- Provide a mechanism to distribute spendable amounts from the Fund;

- Provide the Board with timely monthly statements and performance reports;
- Meet, in person or telephonically, with the Board at least quarterly, and more frequently as needed;
- Monitor the activities of the investment fund; and
- Supply the Board with other reports or information as reasonably requested, including all information necessary for the City's annual audit.

**IX. Monitoring & Review**

The Board shall review the performance of the Advisor(s) on an ongoing basis. This review shall be based on a number of factors, including, but not limited to:

- Adherence to the guidelines and objectives of this document;
- Compliance with the allowable investment types;
- Meeting the investment objectives;
- Comparison of performance against relevant market indices;
- Avoidance of regulatory actions against the firm, its principals or employees;
- Responsiveness to the Board; and
- Quality of reports

**X. Spending Rule**

In order to ensure that the dual goals of preserving the principal of the Fund and generating adequate returns to fund smooth and predictable distributions for current spending, the Board recognizes that a spending rule is necessary. A spending rule provides a formula that controls the amount of money that can be spent from the Fund annually. However, the spending rule is not intended to limit the prerogative of City Council in the choice or selection of spending priorities. The spending rule does allow the Board to manage the portfolio in a prudent fashion, using best practices.

The spending rule percentage for the Fund is initially established at 4.5% of the three year trailing market value. This will be calculated by taking an average of the ending market value of the Fund for the previous twelve calendar quarters. This percentage shall be reviewed each year in light of the performance of the portfolio and market conditions and adjusted as deemed necessary by the Board or as directed by City Council.

**XI. Ratification by City Council**

The Oil & Gas Board Investment Policy and Spending Rule and any subsequent changes shall be presented to City Council for their review and approval.

# Appendix A

## Asset Allocation Table

Asset Class	Minimum %	Maximum %	Target	Benchmark Index
<b>Total Equity</b>	<b>40%</b>	<b>60%</b>	<b>50%</b>	
U.S.	30%	50%	40%	S&P 500
Non-U.S.	0%	20%	10%	MSCI EAFE
<b>Total Fixed Income</b>	<b>25%</b>	<b>45%</b>	<b>35%</b>	Barclays Intermediate US Government/Credit
<b>Cash</b>	<b>10%</b>	<b>20%</b>	<b>15%</b>	3 Month US T-Bill
Local CDs	0%	20%	10%	

We believe this asset mix is appropriate in the context of the portfolio's objectives. Within the specified ranges, the allocation can be modified from time to time in response to perceived changes in relative valuation among the asset classes. During times of extreme market activity, the allocations of this account may fall outside of the stated range for temporary periods of time.

# Appendix B

## INVESTMENT OF SURPLUS FUNDS OF POLITICAL SUBDIVISIONS (EXCERPT)

### Act 20 of 1943

**129.97 Long-term or perpetual trust fund; investment of assets; resolution authorizing investment officer same authority as investment fiduciary under MCL 38.1132 to 38.1140m; conditions.**

Sec. 7. Notwithstanding any law or charter provision to the contrary, if a public corporation has a long-term or perpetual trust fund consisting of money and royalties or money derived from oil and gas exploration on property or mineral rights owned by the public corporation, the governing body of the public corporation may by resolution provide its investment officer with the same authority to invest the assets of the long-term or perpetual trust fund as is granted an investment fiduciary under the public employee retirement system investment act, 1965 PA 314, MCL 38.1132 to 38.1140m.

**History:** Add. 2008, Act 220, Imd. Eff. July 16, 2008.