



# **Alaska Mental Health Trust Authority**

## **Asset Management**

## **Policy Statement**

# Asset Management Policy Statement

## Purpose

The Asset Management Policy Statement (AMPS) specifically delineates the asset management philosophy and practices of the board of trustees of the Alaska Mental Health Trust Authority (the Trust). It has been developed to serve as the management plan for those assets entrusted to the board. The board believes it is essential to adopt a long-term plan by which these assets will be maintained and enhanced through prudent management. The board has adopted the AMPS to serve as that long-term plan, in order that:

- there be a clear understanding on the part of the trustees, staff, beneficiaries, and the public as to the objectives, goals, and restrictions with regard to the management of Trust assets;
- assets be structured and managed in a prudent manner; and
- there be a meaningful basis for performance evaluations of asset classes, managers, and strategies used to achieve the management objectives.

## Background

### *Creation of the Trust*

The Alaska Mental Health Trust Authority (the Trust) was established by Congress under the Mental Health Enabling Act of 1956. The 1956 law included a grant to the State of Alaska of one million acres of land to be used to generate revenues to ensure the development of a Comprehensive Integrated Mental Health Program for the State of Alaska. In the mid 1980s, a class-action citizen lawsuit, Weiss v. State, was filed, alleging the mismanagement of these lands. In 1994, the Alaska Legislature passed legislation that was subsequently approved by the Alaska Superior Court as a settlement of the litigation (the settlement).

## *Settlement Framework*

The settlement reconstituted the Trust with an initial \$200 million in cash and nearly one million acres of land. A seven-member board of trustees was created and charged with the responsibility of administering the Trust. The board is required by statute (AS 37.14.009(a)) to contract with the Alaska Permanent Fund Corporation (APFC) for the management of the cash principal of the Trust and with the Department of Natural Resources (DNR) for the management of its non-cash resource assets. The 1994 legislation required DNR to establish a separate unit, the Trust Land Office (TLO), for this purpose. Trust income allocated for annual mental health program spending and, on a short-term basis, revenue generated by the TLO is managed by the Department of Revenue (DOR).

To carry out this mandate, the board has the responsibility of establishing and maintaining broad policies and objectives for the prudent management of Trust assets. The Board establishes broad policies and sets the direction for asset management in this AMPS.

The board delegates the implementation of these policies to the board's finance committee, resource management committee, executive committee and to staff. In doing so, the board maintains a "top-down" perspective, focusing on important policy-level issues, and maintaining the proper fiduciary perspective and time horizon for analysis of the performance of Trust assets.

The board then directs the financial management of the earnings from the assets of the Trust into programs and projects that are designed to improve the lives of Trust beneficiaries: Alaskans who experience mental illness, developmental disabilities, chronic alcoholism, Alzheimer's disease and related dementia, traumatic brain injury and substance abuse disorders (see AS 47.30).

## *Mission Statement*

The board has adopted the following mission statement for the Trust: The Alaska Mental Health Trust Authority (the Trust) administers the Mental Health Trust to improve the lives of beneficiaries. Trustees have a fiduciary responsibility to protect and enhance trust assets in perpetuity for the beneficiaries. The Trust provides leadership in advocacy for and planning, implementing and funding of the Comprehensive Integrated Mental Health Program; and acts as a catalyst for change.

# Statement of Asset Management Philosophy

The AMPS helps the board effectively supervise, monitor, and evaluate the investment and management of the Trust's cash and non-cash assets. The cash investment program and Trust land and resource management program are defined in the various sections of the AMPS by:

- stating in a written document the board's expectations, objectives, and guidelines for management of the cash and non-cash assets;
- complying, or ensuring compliance, with all applicable fiduciary, prudence, and due diligence requirements that experienced investment professionals and land managers would reasonably utilize, and with all applicable laws, rules, and regulations that may impact Trust assets;
- setting forth an investment structure for the cash assets of the Trust; this structure includes various accounts, asset classes, investment management styles, risk tolerance, asset allocation and acceptable ranges that, in total, are expected to produce a sufficient level of overall diversification and total investment return over the long-term;
- establishing guidelines for management of the Trust's non-cash assets consistent with the TLO's long-term asset management strategy as defined in 11AAC 99.090(c);
- monitoring, evaluating, and comparing the investment performance results achieved by APFC, DOR, and TLO on a regular basis;
- encouraging effective communications between the trustees, staff APFC, DOR, and TLO; and
- establishing a framework to aid trustees in determining the annual available funding amount for protection and enhancement of Trust assets and spending on behalf of the beneficiaries in mental health programs and projects.

This AMPS is formulated upon the board's consideration of the financial implications of a wide range of policies and describes the prudent cash, and non-cash processes that the trustees deem appropriate.

The board recognizes that even though its investments are subject to short-term volatility, it is critical that a long-term investment focus be maintained. This prevents ad-hoc revisions to the board's philosophy and policies in reaction to either speculation or short-term market fluctuations.

## Asset Management Objectives

The asset management objectives of the Trust have been established by the board in conjunction with a comprehensive review of the Trust's current and projected financial requirements. The investment earnings from cash assets and income produced from Trust non-cash assets will be used to protect and enhance the value of Trust assets and implement annual mental health program funding strategies. Accordingly, investment results and Trust land resource management decisions are critical elements in achieving the outcome objectives of the Trust. The overarching asset management objective is to maintain appropriate cash asset allocation and trust land management policies that are compatible with the spending policy while still having the potential to produce positive real returns.

### **Cash Management Objectives**

Specific cash management objectives are to:

- preserve and enhance the purchasing power of the Trust's cash principal and the income generating capacity of the Trust's non-cash asset portfolio;
- achieve a real rate of return (above inflation) of five percent (5%) annually with reasonable and prudent levels of risk; and
- provide a steady, reliable payout stream to ensure funding of program spending goals while maintaining sufficient liquidity in all market environments.

## **Trust Land Management Objectives**

Specific Trust land management objectives are to:

- protect and enhance the non-cash asset value and productivity of Trust property;
- maximize revenues from Trust non-cash assets over time;
- encourage a diversity of revenue-producing uses of Trust non-cash assets;
- manage Trust land prudently, efficiently, and with accountability to the Trust and its beneficiaries; and
- use Trust non-cash assets for beneficiary purposes, when such use is found to be in the best interest of the Trust and its beneficiaries.

# Guidelines and Investment Policy

## **Time Horizon**

So that interim marketplace circumstances and fluctuations will be viewed with appropriate perspective, the investment of the Trust's principal and Budget Reserve account invested at APFC as well as non-cash assets are managed for long term growth over time (generally greater than five years).

Investment strategies for budget reserves invested outside of APFC (currently at DOR) are to be determined by the trustees.

Investment of Trust income allocated for annual mental health program spending as well as the Trust Authority Development Account (TADA) and Trust Facility Maintenance Account is based on a horizon of one year.

## **Risk Tolerance**

The board recognizes the difficulty faced by APFC, DOR and DNR in meeting investment and Trust land resource management objectives because of the uncertainties and complexities of contemporary investment markets and the non-cash asset management operating arena. The board also recognizes that some risk must be assumed to achieve the APFC's long-term investment objectives, the DOR's Budget Reserve investment objectives, and the TLO's land management objectives. Further, in co-mingling Trust cash assets with the Alaska Permanent Fund managed by the APFC, the ability to withstand short and intermediate term market volatility was considered.

## **Performance Expectations**

### ***Cash Managers***

#### **Alaska Permanent Fund Corporation**

APFC management responsibilities for the Trust's principal are provided for in APFC statute and a memorandum of agreement between the Trust and the APFC (APFC MOA).

The board reviews the long-term performance, risk, and liquidity characteristics of the APFC on a periodic basis (but not less than once every three years) and evaluates whether the APFC's asset allocation strategy meets the long-term investment return objective of the Trust with an acceptable level of risk.

#### **Department of Revenue**

The asset allocation for Budget Reserves under management of the Treasury Division is directed by the trustees.

The Department of Revenue Treasury Division holds and manages one half of the Budget Reserve, cash balances of the TADA, and on a short-term basis the revenue generated by the TLO and Trust income allocated by the trustees for spending on the Comprehensive Integrated Mental Health Program.

Investments of the Budget Reserves are made pursuant to guidance provided by staff under the fiduciary direction of the board. In executing their duties, the finance committee shall periodically (not less than every three years) review asset allocation independently or request consultation from outside entities and, if appropriate, recommend the board adopt changes.

The TADA is currently invested alongside the General Fund and other Non-Segregated Investments (GeFONSI). The finance committee shall periodically (not less than every three years) review the cash balances of the TADA in conjunction with projected expected expenditure or reinvestment demand and recommend an asset allocation to the board.

## ***Non-Cash Asset Manager***

### **Trust Land Office**

The TLO manages the Trust's non-cash assets on behalf of the trustees, in accordance with applicable statutes, regulations, and a memorandum of understanding between the Trust and DNR (DNR MOU).

The Trust land resource component of the Trust is made up of about 5,000 land parcels statewide, totaling about one million acres. TLO management responsibilities are provided for in AS 38.05.801, 11 AAC 99, and the DNR MOU.

TLO outcomes are projected for the upcoming budget cycle with annual outcomes addressed in annual TLO budgets approved by the Trustees. While the TLO consults primarily with the resource management committee of the board on specific transactions, consultation can also occur between the TLO and the TAO and between the TLO and the board, in accordance with specific board policies or transaction circumstances.

The performance of direct private equity real estate will be annually evaluated using an index or indices determined by the resource management committee.

General operating expectations are as follows:

- TLO will focus first on land or resources at the high end of their market values ("Best Markets") and then on land or resources with Best Market potential within the next two to ten years;
- land or resources not included above will be considered "Long Term Market" lands, with TLO management emphasis placed on reasonable value preservation and enhancement actions in the interim;



- generally, the TLO will focus on transactions that:
  1. maximize return at prudent levels of risk;
  2. contribute to a diverse assortment of resource activity;
  3. provide ancillary values to the Trust; and
  4. remove or prevent liability risks;
- leases are preferred over sales and, when reasonable to do so, land values should be enhanced before disposal through lease or sale;
- transactions should not harm values of or future opportunities associated with other Trust lands;
- investments in Trust land should compete favorably with the projected long-term total rate of return of the Alaska Permanent Fund Corporation;
- land exchanges may be considered, when associated costs and outcomes can be reasonably established;
- if beneficiary program uses of Trust lands are proposed at rents below fair market value, the increment between proposed rents and fair market value rents will be considered an allocation of Trust revenue and must be approved by the board; and
- lands, structures, and resources may be acquired when the acquisition will add value to the Trust's non-cash asset portfolio or will contribute to the mission of the Trust in another way. All acquisitions will be analyzed on a 'Life Cycle Basis'; defined as the present value of the acquisition cost, the operating income/benefits during the holding periods and the value of the asset at disposition.

In accordance with AS 13.38, 20 AAC 40.610, and this AMPS, TLO revenue will be allocated as follows:

- To Principal: Land sale revenues; royalties from coal, gas, materials, minerals, and oil; perpetual easements; and 85% of revenues from timber sales.
- To Income: Interest from land sale contracts; bonus bids; rents; and 15% of revenues from timber sales.

# Control Procedures

## **AMPS Revisions**

It is not expected that the AMPS will change frequently. In particular, short-term changes in the financial, real estate and natural resource markets and associated operating arenas should not require adjustments to the AMPS.

## **Cash Assets**

APFC & DOR performance will be reviewed at least annually by the finance committee who will report all performance to the board to determine the continued feasibility of achieving the investment and Trust land management objectives and the appropriateness of the AMPS for achieving those objectives.

## **Non-Cash Assets**

The TLO will maintain a level of management capacity necessary to prudently manage and develop Trust non-cash assets over time. It is understood that this component of Trust non-cash asset management represents a significant expense to the Trust.

The duties and responsibilities of the TLO are generally provided for in AS 38.05.801 and more specifically provided for in 11 AAC 99 and the DNR MOU. The specific management principles are provided for in 11 AAC 99.

TLO performance will be reviewed at least annually by the resource management committee which will report all performance to the board.

# Spending Policies

The board has the authority to authorize the expenditure of Trust funds to protect and enhance the value and productivity of Trust assets, for the award of grants and contracts in fulfillment of the Trust's purpose to ensure a Comprehensive Integrated Mental Health Program, and, with legislative approval, the operating expenses of the TAO. This Spending Policy outlines five board objectives:

1. protect and enhance the corpus of the Trust by allocating sufficient resources to ensure that Trust assets are properly managed, including the use of principal allocated to the Trust Authority Development Account, where appropriate, to maximize the value and productivity of Trust non-cash assets;

2. apply smoothing mechanisms to mitigate the effects of short-term market volatility on spending and maintain a reliable funding stream to ensure the support of a Comprehensive Integrated Mental Health Program for the beneficiaries;
3. establish a Budget Reserve account to ensure funding support for the Comprehensive Integrated Mental Health Program is maintained in a difficult market environment;
4. maintain the purchasing power of the Trust principal, including addressing the effects of inflation, by using the reserve model consisting of the Budget Reserve account originally recommended by Callan Associates in 1996; and
5. follow a spending policy based upon a sustainable percentage of investment net asset values and expendable income from Trust land management.

The board recognizes achieving Trust asset management objectives requires adequate resources be allocated for that purpose by reimbursing APFC and DOR, and DNR for the reasonable costs of managing Trust assets.

### *Annual Available Funding Framework*

Having a relatively consistent and predictable funding stream is paramount to ensuring an effective Comprehensive Integrated Mental Health Program. To mitigate the effects of periodic market volatility on funding, the board utilizes smoothing mechanisms to maximize funding consistency.

The following components have been established as a framework to aid trustees in determining the annual available funding amount:

- An annual withdrawal calculation consisting of 4.25 percent of the rolling four year-end average aggregate net asset value (NAV) of the following:
  - Principal invested at APFC<sup>1</sup>
  - Budget Reserve invested at APFC
  - Budget Reserve invested at DOR
- The rolling four year-end average of lapsed appropriations funded from the Settlement Income Account<sup>2</sup>;

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<sup>1</sup> Funds in the Trust Authority Development Account are not included in the payout calculation unless Trustees approve otherwise.

<sup>2</sup> Settlement Income Account AKSAS fund 34046 only. Lapsed appropriations funded from the Facility Maintenance Account are not included in the calculation.

- The rolling four year-end average of expendable income generated by Trust Land Office operations;
- The rolling four year-end average of interest earned on cash held with the General Fund and Other Non-Segregated Investments (GeFONSI) managed by DOR;
- The unobligated/unallocated funds that could have been authorized in previous fiscal years under this framework calculation; and
- Other miscellaneous unrestricted revenues properly deposited into the Trust Settlement Income Account such as contributions from partner agencies and the recovery of prior year expenditures received after the funding appropriation lapsed.

Trustees reserve the right to expend additional funds when circumstances warrant. For instance, if original projections used to build a preliminary budget prove materially inaccurate due to deteriorating market conditions, trustees may elect to authorize funds beyond what the framework above would generally suggest. Concurrently, trustees acknowledge that principal assets must be safeguarded.

The annual withdrawal calculation amount will be transferred to the Settlement Income Account and invested with the GeFONSI with minimal risk on a lump sum or periodic basis by the CFO in consultation with the CEO based on market conditions and cash flow needs.

### *Budget Reserve Guidelines*

In order to fulfill funding requirements during market downturns, a Budget Reserve account will be maintained to help ensure funding availability. Based on a Callan Associates study of the Alaska Permanent Fund and the Alaska Mental Health Trust Fund, the Budget Reserve is set at 400% of the targeted annual withdrawal calculation amount. This reserve amount should be adequate to provide maximum assurance that the Trust will be able to meet annual funding goals.

One half of the Budget Reserve shall be invested by the DOR. The remainder of the Budget Reserve shall be invested by the APFC in the same manner as the Principal.

When APFC experiences gains for a given year, the Budget Reserve at DOR will first be adjusted up to 200% of the current year's targeted annual withdrawal calculation. If additional gains remain, adjustments will be made to the Budget Reserve invested by APFC. When the Budget Reserve is fully funded at both

DOR and APFC, funds may be used to help offset the effects of inflation (“inflation proofing”). The effect of inflation will be estimated by using US Department of Labor Bureau of Labor Statistics CPI-U index<sup>3</sup>.

When the APFC or DOR experiences losses for a given year, the Budget Reserve at DOR will be maintained or adjusted to 200% of the annual withdraw calculation from the Budget Reserve at APFC.

In the event of severe and/or sustained losses whereby the Budget Reserve is insufficient to meet the annual payout while maintaining at least 200% of the current year’s annual withdrawal calculation then the withdrawal rate or amount may be reviewed by the trustees.

Full or partial inflation proofing may be facilitated by one of the following methods:

- Inflation proofing permanent transfer (official non-spendable transfer)
  - Upon notification by the CFO that trustees have performed an official and permanent inflation proofing, APFC will initiate an accounting entry to irretrievably transfer funds from Budget Reserves to the non-spendable principal account.
- Inflation proofing assignment (notional transfer)
  - No official entries are necessary as funds remain in the Budget Reserve account at APFC, however the board is officially on record assigning the balance perpetually just as though the funds were principal. This balance is not factored into the base goal to maintain 400% of the targeted withdrawal in reserves. The notional inflation proofing subaccount of Budget Reserves may theoretically be utilized by the board under draconian market circumstances.

### *Trust Authority Development Account Guidelines*

The value and productivity of Trust cash and non-cash assets must be maximized through the reinvestment of Trust principal where appropriate. This includes investments made through Program Related Investments (PRI), the Resource Management Strategy (RMS) or other programs approved by trustees. To achieve this objective, the Board will maintain a Trust Authority Development Account (TADA) to use Trust principal to exchange one principal asset for another, to maintain or enhance the value of the Trust’s existing non-cash asset portfolio, either through prudent investments in non-cash assets already owned by the Trust or through the acquisition of additional assets. Principal assets in the TADA may also be used to acquire assets that enhance

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<sup>3</sup> Consumer Price Index All Urban Consumers; U.S.; All Items; 1967=100  
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the capacity of the TADA may also be used to acquire assets that enhance the capacity of the state's mental health program. This may be accomplished through the financing of projects , purchase/lease of assets, exchange or resale.

Recommendations for expenditure from the TADA will be noticed in the same manner as other Trust expenditures, including presentation to appropriate Trust committees and final approval by a committee or the board of trustees, as provided for in the Trust bylaws. Recommendations will be based upon a specific work plan with identified priorities.

# Definitions

For purposes of ease of administration and understanding of this Asset Management Policy Statement, the following terms are defined or clarified:

**APFC:** The Alaska Permanent Fund Corporation manages the cash assets of the Alaska Mental Health Trust Authority under the APFC board's asset allocation policy and its investment policies and guidelines for major asset classes.

**ASSETS:** Consists of the cash and non-cash assets of the Alaska Mental Health Trust Authority, including property and resource assets acquired by the TLO on behalf of the Trust.

**BOARD:** The governing body of the Alaska Mental Health Trust Authority established by AS 47.30.016.

**BUDGET RESERVE:** Budget Reserve is set at 400% of the targeted annual disbursement amount. This reserve amount should be adequate to ensure the Trust's ability to meet its spending goals in a difficult market environment and to ensure liquidity in future years. The budget reserve is maintained both within the state treasury (in GASB fund 34047) as well as the Alaska Permanent Fund Corporation.

**CHIEF EXECUTIVE OFFICER (CEO):** The staff position as defined by AS 47.30.026 serving the board as the chief executive officer of the Alaska Mental Health Trust Authority.

**TRUST SETTLEMENT INCOME ACCOUNT:** The account in which income available for appropriation and expenditure is deposited (and from which agencies receiving MHTAAR funded appropriations expend). The account is maintained on the state accounting system as GASB fund 34046.

**TRUST AUTHORITY DEVELOPMENT ACCOUNT:** A temporary principal account maintained by the board to facilitate periodic principal exchanges and to enhance the value of the Trust's assets. It is also the holding place for cash principal until it is transferred to the APFC for investment alongside the Alaska Permanent Fund. The account is maintained on the state accounting system as GASB fund 34045. Prior to September 2014, this account was referred to as the Trust Land Development Account.

**TRUST FACILITY MAINTENANCE ACCOUNT:** A component of the Settlement Income Account where a portion of facility rents are deposited to finance operations and maintenance on buildings owned by the Trust. The account is maintained on the state accounting system as GASB fund 34048. The account was originally authorized by Resolution 05-04.

**TRUST LAND PORTFOLIO:** The non-cash assets of the Alaska Mental Health Trust Authority that are managed by the Trust Land Office, including improved properties and facilities.

**SETTLEMENT:** The statutes, settlement agreement, letters clarifying the settlement agreement, and the final Superior Court order creating and approving the settlement of Weiss v. State of Alaska.

**STAFF:** The CEO, Trust Land Office Executive Director, all employees of the Trust and the Trust Land Office.

**TRUST:** The Alaska Mental Health Trust established by Congress under the Mental Health Enabling Act of 1956.

**TRUST AUTHORITY:** The Alaska Mental Health Trust Authority established by AS 47.30.011.

**TRUSTEE(S):** The board of trustees of the Trust Authority, either collectively or individually.

**TRUST ADMINISTRATIVE OFFICE (TAO):** The office with responsibility for providing support to the chief executive officer and board of trustees in management of Trust financial assets and in assuring development of the Comprehensive Integrated Mental Health Program.

**TRUST LAND OFFICE (TLO):** The office with responsibility for management of the Trust non-cash assets (property and natural resource assets) established within the Department of Natural Resources under AS 44.37.050.

**TRUST LAND OFFICE (TLO) EXECUTIVE DIRECTOR:** The staff position serving the commissioner of the Department of Natural Resources in conjunction with the board as the executive director of the Trust Land Office.