

ALASKA MENTAL HEALTH TRUST AUTHORITY

FINANCE COMMITTEE MEETING

April 22, 2020

8:30 a.m.

WebEx Videoconference/Teleconference

Originating at:

3745 Community Park Loop, Suite 120

Anchorage, Alaska

Trustees Present:

Laraine Derr, Chair

Rhonda Boyles

John Sturgeon

Ken McCarty

Chris Cooke

Verne' Boerner

Anita Halterman

Trust Staff Present:

Mike Abbott

Steve Williams

Carol Howarth

Miri Smith-Coolidge

Kelda Barstad

Luke Lind

Michael Baldwin

Carrie Predeger

Katie Baldwin-Johnson

Jimael Johnson

Valette Keller

Eric Boyer

Autumn Vea

Allison Biastock

Katie Vachris

Kat Roch

Trust Land Office:

Wyn Menefee

Jusdi Doucet

Marisol Miller

Also participating:

Angela Rodell; Erin O'Boyle; Gayle McDonough; Charlene Tautfest; Rebeka Carpenter; Sheila Harris; Stephanie Hopkins.

PROCEEDINGS

CALL TO ORDER

CHAIR DERR called the meeting to order and began with a roll call.

MR. ABBOTT stated that there were six committee members present.

CHAIR DERR asked for any announcements. There being none, she moved to approval of the agenda.

APPROVAL OF AGENDA

MOTION: A motion to approve the agenda was made by TRUSTEE STURGEON; seconded by TRUSTEE BOERNER.

There being no objection, the MOTION was approved.

ETHICS DISCLOSURES

CHAIR DERR asked for any ethics disclosures.

TRUSTEE McCARTY respectfully submitted an ethics consideration statement. "I am the founder and executive director of Discovery Cove Recovery and Wellness Center which is a for-profit community mental health care facility. It employs licensed clinical therapists, physicians, and psychiatrists. Its outreach directly affects Trust beneficiaries whether through services of mental health, developmental disabilities, or substance use. Our opioid, our medication treatment program reaches beneficiaries from Juneau to Nome. Through appointment by the Governor and confirmation by the Legislature of a vote of 59 to 1, with full knowledge of my background, I am honored to be a trustee of the Mental Health Trust. If in due course of discussions regarding Trust matters which may be seen to have a conflict of interest due to my position as executive director of Discovery Cove, that I understand that I may not be able to participate, thus, to cease the direction of the Chair and trustee bodies as to whether I should recuse myself for such individual matters that may be discussed on our current agenda and throughout this current meeting. Thank you."

CHAIR DERR thanked Trustee McCarty and stated that if anything came up in regard to his organization, it will be decided at that time on whether he would be able to vote or not. She asked for any other ethics disclosures. There being none, she moved to the approval of the minutes of the January 3, 2020 meeting.

APPROVAL OF MINUTES

MOTION: A motion to approve the minutes of the January 3, 2020 Finance Committee meeting was made by TRUSTEE COOKE; seconded by TRUSTEE HALTERMAN.

There being no objection, the MOTION was approved.

CHAIR DERR moved to the next item on the agenda, and recognized Angela Rodell.

PLANNING ITEMS

MS. RODELL thanked all and began by explaining, historically, how the asset allocation for the

Fund had changed over the years. She stated that asset allocation is where the cash is, which allows the Fund to continue to generate returns, and also spreads risk around. Having this diverse asset allocation allows the management of returns and risk in a more prudent manner. She moved to the global economy and stated that 73 percent of the Fund is in the United States. She talked about the effect that the pandemic has had on the global markets and that some will be able to recover sooner, and we will be able to take advantage of the recovery efforts that happen. She added that the results of the real impact of what is happening to companies on their revenues, and their ability to maintain their business models will be seen in July, the second quarter of calendar year 2020. She moved to the value of the Mental Health Trust assets that the Fund manages. As the Fund grew, the funds managed on behalf of the Mental Health Trust have grown. She explained the lows as they came about in March, and then stated that they are coming back up. On April 30th, an updated balance on that Mental Health Trust balance should be provided.

CHAIR DERR thanked Ms. Rodell and called a break.

(Break.)

CHAIR DERR called the meeting back to order and recognized Carol Howarth.

FINANCIAL DASHBOARD

MS. HOWARTH stated that she would go through the dashboard by first focusing on expenditures, then the receipts, and finally the fund balances. She talked about how the process went in regard to the total program number and explained how it related to the COVID-19 special funding. She stated that the team in the process looked at the existing grants issued with a good communication between parties and, given the current situation, those funds will be expanded. She moved on to Trust receipts and began with the Trust Land Office which has two sources of income: One is principal income that goes directly to the Permanent Fund; the other, Trust Land Office income, goes into the ultimate spendable account. She recounted the Trust Land Office's revenue to date, and moved to the investment activity.

TRUSTEE COOKE found the new dashboard easier to follow and understand, with the ability to compare categories.

MS. HOWARTH gave credit to Andy Stemp and Sarah Morrison, who got the report to this point.

CHAIR DERR thanked Sarah for stepping in for Mr. Stemp and doing an excellent job. She asked Mr. Abbott to continue.

FY2021 BUDGET UPDATE

MR. ABBOTT moved into the conversation about what the changes in the financial position mean for the near-term revenue streams. He stated that the impact on revenues for FY21 between what was anticipated in January and what is anticipated now is about \$650,000 less revenue for the fiscal year that will start July 1st. He explained that the reason for the small change is that a relatively conservative averaging process was used so there is no overreaction in any given year to either good or bad news. The same thing is true of investment earnings. The impact of that overall means that for all of the different revenue types, using the four-year

averaging methodology that the trustees approved many years ago, is that the spendable revenue in FY21 is only 2 percent less than what it was thought to be a few months ago. He added that it is entirely possible that those numbers will get better if investment performance is even marginally positive for the rest of the current fiscal year. He continued that the reason that it is not necessarily impactful in the near term is that the revenues anticipated for FY21 have not been fully allocated for spending yet.

CHAIR DERR moved to Harvest Capital on the agenda.

HARVEST CAPITAL

MS. HOWARTH introduced Erin O'Boyle and Gayle McDonough from Harvest Capital and stated that they joined as a third-party real estate investment adviser to do an objective analysis of the Trust Land Office's real estate portfolio.

MS. O'BOYLE stated that she is the managing partner of Harvest Capital Partners and appreciated the opportunity of being the real estate adviser, supporting the great mission of serving the beneficiaries. She stated that the presentation would cover the role of Harvest Capital, the fiduciary evaluation of the portfolio, an overall portfolio overview, the findings, and the recommendations. She continued that she is a founder and managing partner of Harvest, which is an SEC investment registered adviser, a minority women-owned business enterprise. She added that she had a master's in real estate from MIT.

MS. McDONOUGH stated that she was also a graduate of MIT and has 30-plus years in investment management with a background in acquisitions, dispositions, asset management portfolios of property and advising projects.

MS. O'BOYLE stated that their duty was to advise, advocate, and protect the Trust to maximize value of the assets; provide leadership in advocacy and planning to maximize the total return for the funding of programs; and, as a SEC registered adviser, they have to fulfill their obligation as a fiduciary to act in the Trust's best interests in making recommendations for those best interests. She continued that there are three primary criteria in the evaluation: Portfolio quality, management, and performance. She reported that on portfolio quality, the assets were bought at the right time, at good prices, and in good, solid submarkets. She continued on to management and stated that they have worked closely with the TLO staff and have met all the property managers. She added that they were on regular calls with the team as they have been managing through this crisis, and they are strong capable managers. She moved to performance and stated that the legislative audit did not evaluate performance. Their scope was to evaluate processes and capabilities, establish guidelines, policies, following the enabling legislation. It also cited a lack of guidance to consider the real estate holdings in the context of the allocation of the real estate through the Alaska Permanent Fund. She stated that she cannot speak to past events, but she can speak to the ownership of a portfolio and the fiduciary responsibility to recommend investment decisions. She continued that the income stream has proven to be exceptionally durable at a time when liquidity and durability are at a premium.

MS. McDONOUGH went through the portfolio beginning with Israel Road in Tumwater, Washington, which is 100 percent leased credit tenants; next was North Rulon in Ogden, Utah, 100 leased to the IRS, a long-term credit lease; San Pedro Avenue in San Antonio, Texas, which is 97 percent leased; True Source lease renewal has been complete; and the Marriott Worldwide

renewal is fully negotiated and out for signature with the tenant. She stated that next was Amberglenn Boulevard, Austin Texas, 97 percent leased; Ridgepoint Drive in Austin, Texas, is 100 percent leased; Cordova Street in Anchorage, 82 percent leased, and 97 percent occupied; Commercial Drive, Anchorage, Alaska is 100 percent leased to Cummins Northwest.

MS. O'BOYLE stated that the valuations of the portfolio, from the last external appraisals to this valuation, went from \$95 million to \$99 million. She continued that one of the findings included that the portfolio debt does not follow best practices. The practices that it did not follow at this loan to value was interest only, with other provisions such as loan extensions, favorable prepayment provisions, et cetera. She added that an extensive cash-flow analysis was done with the team and is appended in the packet. She talked about the flexibility in financing interest only to make whatever amortization payments desired that is not contractually required and is a big difference. She continued that flexibility is especially important. The portfolio has been financed with extremely high quality life companies and banks, and those are very preferred lenders for real estate. She stated that the final recommendation is to refinance the portfolio with interest-only debt, conservatively 3 to 3.5 percent, with flexible prepayment terms that would increase the cash flow by almost \$20 million compared to the existing financing. She continued that if it is not refinanced, then there is a need to fund the maturing loans. She suggested engaging a mortgage broker to market the portfolio to lenders and negotiate best terms, and then consider a portfolio loan instead of individual loans.

MS. McDONOUGH went through the final summary and stated that this was done to highlight the differences between the scenarios and to show that there can be some cash flow benefits. Scenario A provides \$26 million to the Trust over ten years. Scenario B models the existing debt and provides roughly \$19 million to the Trust over the same ten years. Scenario C is that recommended refinance which provides approximately \$45 million for the Trust over those same ten years.

MS. O'BOYLE talked about the impact of COVID-19 on the debt market. She stated that they appreciated the opportunity to present.

CHAIR DERR thanked Harvest and called a break.

(Break.)

CHAIR DERR called the meeting back to order and asked Mr. Menefee for a presentation on COVID-19 effects on real estate cash flows.

COVID-19 EFFECTS ON REAL ESTATE CASH FLOWS

MR. MENEFEE talked about the impacts on commercial real estate properties with the COVID-19 pandemic going on. He stated that it is having an effect on properties by restricting cash flows for businesses, and then adding to business uncertainty. That is the main focus of why COVID affects business. The uncertain economy and the future business strength is all uncertain. Businesses that depend on tourism or doing business with people in person are being affected more. He explained that some of the properties are government tenants which were considered essential services, and the Trust benefited from that. He continued that having this affecting the businesses means that it could affect the lease renewal process and extension negotiations. It reduces the confidence in being able to say that a vacated space can be filled right away because

of dependence on the market of the local conditions. He added that there will be a bit of a dip in revenue in the commercial real estate investment properties. The revenue projections have been revised as the year goes on, and we are starting to have to set aside cash reserves to potentially deal with vacancies, rent abatements, tenant improvements for people that do early lease renewals or extensions. He moved on to the 2021 real estate budgets, and talked about how the whole document would flow structurally. In order to expend the Trust funds to pay for all the operating and capital expenses and such, we need to request approval. He continued that Motions 2 and 3 are a combination dealing with expenses not covered by the rents. He asked for a motion.

MOTION: A motion that the Finance Committee recommends that the Alaska Mental Health Trust Authority Board of Trustees concur with the recommendation to approve the incremental building expenditures totaling \$10,405,837 budgeted for the fiscal year 2021 to be paid by the property manager from rents and other income collected from the properties was made by TRUSTEE COOKE; seconded by TRUSTEE HALTERMAN.

MS. MILLER stated that for proposed Motion 1, it is anticipated that fiscal year gross revenues from both rents and program-related investment properties are \$11,799 million. She continued that they are anticipating that to both maintain and service the properties, pay the property managers everything required to keep the buildings in proper functioning capacity, will be \$10,405,836.86. She talked about the methods used to come up with the needs of the properties to keep them in the best operating function.

MR. ABBOTT clarified that this was about two groups of properties in one motion and not just the investment properties. He added that the list of the properties are in the packet.

CHAIR DERR asked for any other questions or comments. She called the vote.

After the roll call vote, the MOTION was approved (Trustee Boyles, yes; Trustee McCarty, yes; Trustee Cooke, yes; Trustee Halterman, yes; Trustee Boerner, yes).

CHAIR DERR asked Mr. Menefee to do the overview for the next two motions.

MR. MENEFEE stated that there is not enough rent to pay the property expenses, and we are looking at pulling money from the Central Facility Fund. Essentially, Motion 2 is to approve the use of CFF funds to pay for some of the expenses.

MS. MILLER explained that there is a request for \$15,000 in capital improvements for the primary tenant at the Trust Authority Building, and the additional funds will be for operating and maintaining the building, keeping it up to ADA standards. She continued that there is a request for \$53,032 to make capital improvements that are needed to the building for the Anchorage School District who occupy much of the first floor of the Trust Authority Building.

MR. ABBOTT explained that the reason the TAB is a poor-financially-performing asset is that the Trust Authority does not pay rent. Half of the building that the school district does not rent is utilized by the Trust Authority, which is why the building barely breaks even on an operating basis and does not generate enough additional income to support periodic capital improvements.

CHAIR DERR asked for a motion.

MOTION: A motion that the Finance Committee recommends that the Trust Authority Board of Trustees approve funding the expenditures for the noninvestment-program-related real estate and REMP real estate Trust-funded properties, in the amount not to exceed \$53,032 for the fiscal year 2021 from the Central Facility Fund, which appropriation shall not lapse, was made by TRUSTEE COOKE; seconded by TRUSTEE HALTERMAN.

CHAIR DERR called the vote.

After the roll call vote, the MOTION was approved (Trustee Boyles, yes; Trustee McCarty, yes; Trustee Cooke, yes; Trustee Halterman, yes; Trustee Boerner, yes; Trustee Sturgeon, yes; Trustee Derr, yes).

CHAIR DERR moved to Motion 3.

MOTION: A motion that the Finance Committee recommends that the Trust Authority Board of Trustees instruct the CFO to transfer up to \$53,032 to the third-party property manager, as requested by the TLO, for capital improvements to the noninvestment/program-related real estate and REMP real estate Trust-funded properties was made by TRUSTEE COOKE; seconded by TRUSTEE HALTERMAN.

CHAIR DERR called the vote.

After the roll call vote, the MOTION was approved (Trustee Boyles, yes; Trustee McCarty, yes; Trustee Cooke, yes; Trustee Halterman, yes; Trustee Boerner, yes; Trustee Sturgeon, yes; Trustee Derr, yes).

MR. MENEFEE thanked the trustees for the consideration and, with this approval, we will continue to keep the buildings in good order and try to keep them filled.

CHAIR DERR asked for the next item on the agenda.

REAL ESTATE PORTFOLIO REFINANCE

MR. ABBOTT replied that the next item is the refinance discussion. He stated that staff is not recommending an approval of a specific strategy or specific refinance approach, but would like the committee to direct staff to continue to develop options for the trustees to consider. He suggested the motion be read and then discussed.

TRUSTEE COOKE questioned the necessity of a motion.

CHAIR DERR asked if trustee direction to staff would come from the motion or would it be better to just discuss it.

MR. ABBOTT replied that talking about it would be fine.

CHAIR DERR stated that there would be discussion, and then direction as to what the trustees

wanted. She recognized Ms. Howarth.

MS. HOWARTH stated that staff highly valued the perspectives and recommendations that Erin O'Boyle and Gayle McDonough presented. She continued that two things happened with this proposal: One explored the interest-only refinance of the assets. Looking at this from a portfolio perspective gives the Trust the opportunity to look at the impact of restructuring the debt on the cash flow. She added that interest rates are lower than when the initial mortgages were utilized, and there are two properties that have balloon payments coming up. Third is that the equity in the property is very high, so the loan to value is good. She went through some of the scenarios on the cash flow and how they affect the operation. She added that it is critical to understand the cash-flow implications.

CHAIR DERR asked the trustees for their individual thoughts and comments on the recommendations from Harvest. After the discussion, she asked Ms. Howarth if she had an idea of what to be prepared for in May.

MS. HOWARTH recapped that there is a lot of concern about the market with regards to real estate with a need to put this in a broad context. Some political factors have to be factored in, and we need to do a professional evaluation because there are some options that might have been missed.

MR. ABBOTT stated that this was very helpful and gives staff a chance to deliver products going forward that meet the trustees' expectations, and they hopefully address trustees' concerns.

CHAIR DERR moved to the inflation-proofing discussion.

INFLATION-PROOFING DISCUSSION

MR. ABBOTT stated that in January the reserves were in excess of the 400-percent target, which triggered a conversation about inflation-proofing options. He continued that since then the markets have changed radically and the value of the investments have declined significantly. He added that the reserves now sit well below the target at which inflation-proofing would be considered, and it is now a moot point.

MS. HOWARTH stated that one of the questions to think about is this kind of a standard protection, or do we need to look for strong protection for those beneficiaries long term through inflation-proofing, because that would be more aggressive.

CHAIR DERR asked for any questions from the trustees on inflation-proofing. There being none, she moved to the investment policy.

INVESTMENT POLICY UPDATE

MR. ABBOTT moved to the packet and the list of the trustee obligations related to reviewing and overseeing the investment allocation, investment performance, essentially the investment behavior. He stated that Ms. Howarth developed a presentation in a calendarized version of when these different opportunities will be brought in to weigh in on the asset management and asset performance. He continued that some are new requirements and others are legacy requirements that have been worked on, but we do want to get on track with an updated asset management policy statement.

MS. HOWARTH stated that she could use some thought and guidance on the Central Facility Fund which did emerge in the discussion.

CHAIR DERR asked for anything else to come before the Finance Committee before adjournment. There being nothing, she asked for a motion to adjourn.

MOTION: A motion to adjourn was made by TRUSTEE BOERNER; seconded by TRUSTEE STURGEON.

There being no objection, the MOTION was approved.

(Finance Committee meeting adjourned at 12:53 p.m.)