

## MEETING AGENDA

**Meeting:** Finance Committee  
**Date:** March 5, 2021  
**Time:** 1:30 PM  
**Location:** online via webinar and teleconference  
**Teleconference:** (844) 740-1264 / Meeting Number: 177 535 7374 # / Attendee Number: #  
<https://alaskamentalhealthtrust.org/>  
**Trustees:** Anita Halterman (Chair), Verné Boerner, Rhonda Boyles, Chris Cooke, Brent Fisher, Annette Gwalthney-Jones, John Sturgeon

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Friday, March 5, 2021

Page No.

**1:30 pm**     **Call Meeting to Order (Anita Halterman, Chair)**

Roll Call  
Announcements  
Approve Agenda  
Ethics Disclosure

**1:35**     **Inflation Proofing the Trust Fund**

4

**3:30**     **Adjourn**

## Future Meeting Dates

### Full Board of Trustee / Program & Planning / Resource Management / Audit & Risk / Finance

(Updated – February 2021)

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|--|----------------------------|------------------------|
| • Audit & Risk Committee                   | April 21, 2021             | (Wed)                  |
| • Finance Committee                        | April 21, 2021             | (Wed)                  |
| • Resource Mgt Committee                   | April 21, 2021             | (Wed)                  |
| • Program & Planning Committee             | April 21, 2021             | (Wed)                  |
| • Full Board of Trustee                    | May 26, 2021               | (Wed) – TBD            |
|  |                            |                        |
| • Program & Planning Committee             | July 27-28, 2021           | (Tue, Wed)             |
| • Audit & Risk Committee                   | July 29, 2021              | (Thu)                  |
| • Resource Mgt Committee                   | July 29, 2021              | (Thu)                  |
| • Finance Committee                        | July 29, 2021              | (Thu)                  |
| • Full Board of Trustee                    | August 25-26, 2021         | (Wed, Thu) – Anchorage |
|  |                            |                        |
| • Audit & Risk Committee (tentative)       | October 20, 2021           | (Wed)                  |
| • Finance Committee (tentative)            | October 20, 2021           | (Wed)                  |
| • Resource Mgt Committee (tentative)       | October 20, 2021           | (Wed)                  |
| • Program & Planning Committee (tentative) | October 21, 2021           | (Thu)                  |
| • Full Board of Trustee                    | November 17-18, 2021       | (Wed, Thu) – Anchorage |
|  |                            |                        |
| • Audit & Risk Committee                   | January 5, <b>2022</b>     | (Wed)                  |
| • Finance Committee                        | January 5, <b>2022</b>     | (Wed)                  |
| • Resource Mgt Committee                   | January 5, <b>2022</b>     | (Wed)                  |
| • Program & Planning Committee             | January 6, <b>2022</b>     | (Thu)                  |
| • Full Board of Trustee                    | January 26-27, <b>2022</b> | (Wed, Thu) – Juneau    |

## Future Meeting Dates Statutory Advisory Boards (Updated – February 2021)

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### **Alaska Mental Health Board / Advisory Board on Alcoholism and Drug Abuse**

AMHB: <http://dhss.alaska.gov/amhb/Pages/default.aspx>

ABADA: <http://dhss.alaska.gov/abada/Pages/default.aspx>

Executive Director: Bev Schoonover, (907) 465-5114, [bev.schoonover@alaska.gov](mailto:bev.schoonover@alaska.gov)

- March 10-12, 2021 – via zoom (tentative)
- Executive Committee – monthly via teleconference (Fourth Wednesday of the Month)

### **Governor’s Council on Disabilities and Special Education**

GCDSE: <http://dhss.alaska.gov/gcdse/Pages/default.aspx>

Executive Director: Kristin Vandagriff, (907) 269-8999, [kristin.vandagriff@alaska.gov](mailto:kristin.vandagriff@alaska.gov)

- May 13-14, 2021 – via zoom

### **Alaska Commission on Aging**

ACOA: <http://dhss.alaska.gov/acoa/Pages/default.aspx>

Executive Director: Lisa Morley, (907) 465-4879, [lisa.morley@alaska.gov](mailto:lisa.morley@alaska.gov)

- TBD

## MEMO

**To:** Anita Halterman, Finance Committee Chair  
**Through:** Mike Abbott, Chief Executive Officer  
**From:** Carol Howarth, Chief Financial Officer  
**Date:** February 26, 2021  
**Re:** Inflation Proofing

### REQUESTED MOTION

*The Finance Committee recommends that the board of trustees approve the transfer of \$120,280,300 from the Alaska Mental Health Trust Authority budget reserve account to the Alaska Mental Health Trust Authority principal account managed by the Alaska Permanent Fund Corporation.*

#### **Background**

The Authority has an obligation to ensure mental health trust resources are available to support the needs of both current and future beneficiaries. AS 37.14.009 and AS 47.30.036(1) guide the Authority's responsibilities to future beneficiaries. To meet this obligation the Authority must maintain near-term spending discipline in order to take steps necessary to preserve the real value of Trust resources in perpetuity.

The Authority has established policies that are designed to generate the resources necessary to inflation-proof the Mental Health Trust Fund ("Trust Fund" or "principal"<sup>1</sup>). The spending policy is the most important tool available to the Authority to ensure that resources are available decades from now to support the mission of the Trust. An equally important tool can be designated inflation-proofing of the Trust Fund. With inflation proofing, which will help ensure that income can increase in line with inflation, the buying power of the principal is irrevocably protected.

By setting an annual withdrawal of 4.25%, the Trust Fund and reserve funds can be expected to generate enough earnings in excess of the payout to make periodic transfers to the Trust Fund to offset the impact of inflation. The investment earnings in excess of the 4.25% annual payout are designated as Trust reserves and are not reinvested in the

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<sup>1</sup> The Alaska Mental Health Trust Fund, or Trust Fund is designated by the Alaska Permanent Fund Corporation as "principal."

Trust Fund without express board approval. Annual earnings cannot be perfectly predicted, but over time, the investment earnings (above the 4.25% payout) are very likely to produce sufficient funds to allow Trustees to protect the real value of the Trust Fund.

Although reserves can be used for virtually any Trust approved purpose, inflation-proofing is specifically identified as a Trust option in statutes. From 1994 - 2005 the Authority prioritized its responsibility to future beneficiaries when Trust reserve balances were high enough to support inflation-proofing. Since 2005 the Authority has not made significant inflation-proofing deposits into the Trust Fund. In part, the lack of inflation-proofing during this period was due to the dramatic loss in value of Trust reserves in FY2009 and FY2010 due to investment market declines and the subsequent strategy to further diversify Trust investments. The last time the Trust Fund was considered fully inflation-proofed was 2005.

A summary of inflation-proofing actions is provided in the following table.

<b>Year</b>	<b>Inflation-Proofing Transfer (\$)</b>
FY1995	\$ 3,533,000
FY1998	6,910,543
FY2000	41,544,000
FY2003	11,059,800
FY2005	15,337,401
FY2008	2,436,354
FY2018	5,000,000
<b>Total</b>	<b>\$85,821,098</b>

**Trust Reserves**

In 2004, based on guidance from our investment advisor Callan Associates<sup>2</sup>, the Authority established a target for Trust reserves in the its Asset Management Policy Statement (AMPS). The Trust reserves target was set at 400% of the most recent year’s annual payout. This level was established to provide high confidence that the Trust would have enough reserves to maintain Trust funding for important beneficiary-serving programs during periods of significant declines in investment values.

The AMPS directs the Authority to divide the investment of the reserves between the Alaska Permanent Fund Corporation (APFC) and the state’s Department of Revenue

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<sup>2</sup> Founded in 1973, Callan Associates is one of the largest U.S. independent investment consulting firms, advising both governments and the private sector on investment strategy, performance and risk monitoring. Its clients include APFC and the State’s Treasury department, as well as entities such as CalPERS.

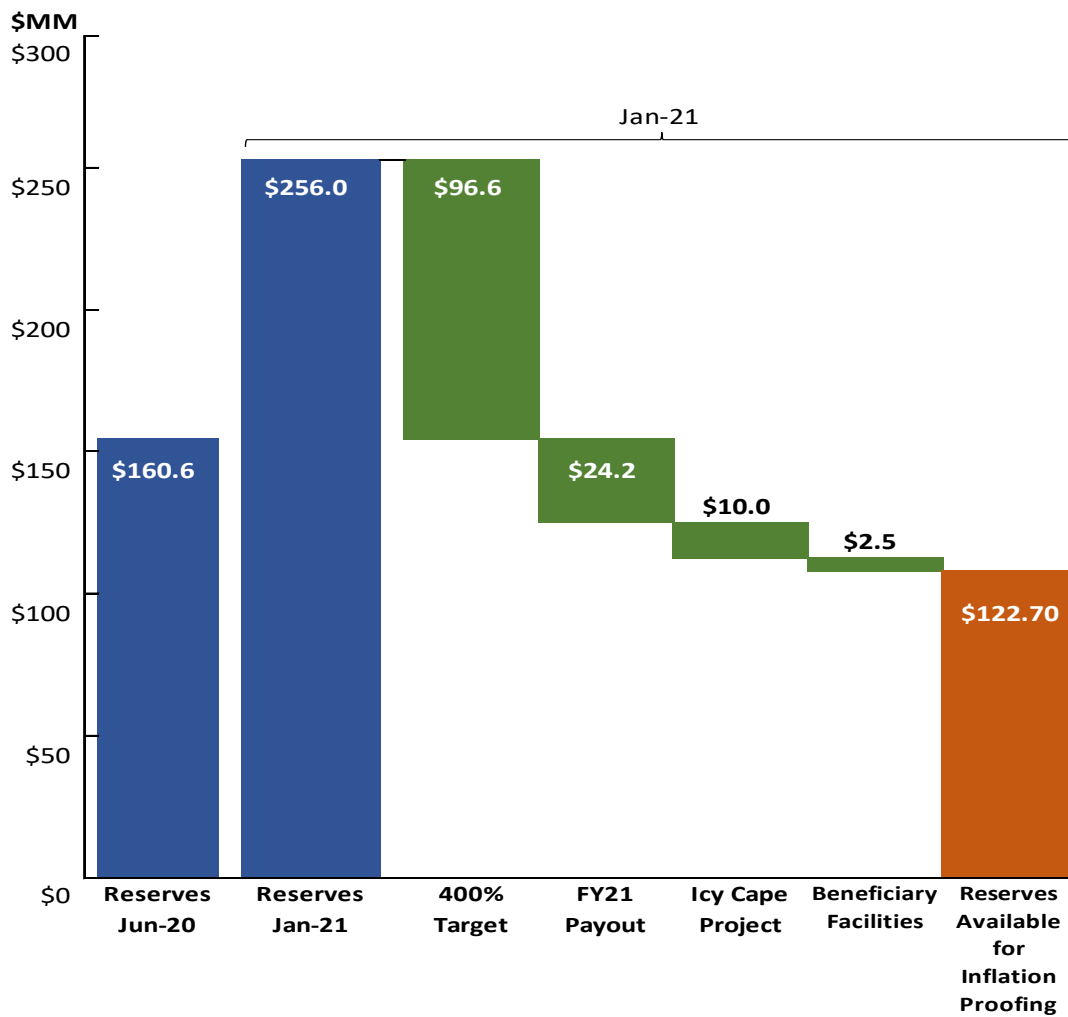
(DOR) in separately managed portfolios. The reserves managed by APFC are co-mingled with the Trust Fund, which is co-mingled with the Alaska Permanent Fund. The reserves managed by DOR are in a portfolio customized for the Trust. Historically, the DOR returns are slightly lower than APFC due to a shorter investment horizon.

Once the budget reserve target is achieved, the AMPS directs the Authority to consider inflation-proofing the Trust Fund with any excess reserves. At the end of FY20, Trust Reserves stood at \$160.6MM. Since then, the reserve balance has grown to \$256.0MM as of January 31, 2021. After adjusting for the 400% reserve target (\$96.6MM), the FY21 payout (\$24.2MM), reservations for Icy Cape development approved in January 2021 (\$10MM), and beneficiary facilities approved in FY19 (\$2.5MM), the reserves available for inflation proofing totaled \$122.7MM.

### Trust Budget Reserves

#### Balances, Obligations, Reservations, and Funds Available for Inflation Proofing

FY2020 Balance and Status as of January 31, 2021



\* Beneficiary Facilities reservation, which is subject to Trustee approval, sets aside funds to acquire property(s) to support beneficiary serving partners (approved by Trustees in November, 2018).

According to the AMPS, the effect of inflation is to be estimated using the U.S. Department of Labor Bureau of Labor Statistics CPI-U index<sup>3</sup>. To match the purchasing power of the original \$200MM and subsequent contributions to the Trust Fund as of December 31, 2020, a permanent transfer of \$120,280,300 is needed.

	<b>As of December 31, 2020</b>
Initial Trust Fund Contribution (FY95)	\$200,000,000
Subsequent Trust Fund Contributions	163,990,000
Total Trust Fund Contributions	364,026,000
Inflation Proofing (FY95-FY18)	85,821,100
<b>Trust Fund</b>	<b>\$449,847,100</b>
Fully Inflation Proofed Trust Fund	\$570,127,400
<b>Inflation Proofing Required</b>	<b>\$120,280,300</b>

**Alternative Approach**

Another option for preserving long-term value of the Trust’s assets over time is “soft” inflation-proofing (“hard” inflation-proofing is the approach described previously). In this approach funds need not be transferred to the Trust Fund to inflation proof. Funds may stay in reserves. By managing spending at a rate below the real rate of return, the growth of the total invested cash assets—principal and earnings—builds a total fund balance that has an increasing purchasing power and supports spending growth<sup>4</sup>. One evaluates the market value of budget reserves and the Trust Fund against what the total balance “should be” if the AMPS is followed. As of Fiscal Year-End 2020, there was a \$33,572,000 shortfall in funding. As of December 31, 2020, there was a surplus of \$23,496,000.

The “soft” inflation-proofing approach is not recommended at this time. To ensure long-term protection of the Trust’s ability to support beneficiaries, funds must be transferred to the Trust Fund and thereby receive the protection against spending provided by the Alaska Mental Health Trust statutes.

<sup>3</sup> <sup>3</sup> Alaska Mental Health Trust Authority. (2019). *Asset Management Policy Statement, Adopted August 29, 2019*. Retrieved from: <https://alaskamentalhealthtrust.org/wp-content/uploads/2019/08/AMPS-adopted-Aug2019.pdf>.

<sup>4</sup> For example if in a given year inflation is 2%, the return target is a 5% real return, the Trust needs to earn 7%. (7% less 2% inflation = 5% real rate). If the planned payout is 4.25%, after the payout, there should be an increase of 2.75% in reserve balances. (5% real rate less 4.25% = 0.75% left over, yet the Trust must also maintain inflation proofing of 2%, for a total of 2.75% increase).

### **Conclusion and Recommendation**

The Trust is in a sound financial position, having maintained purchasing power through its spending discipline and adherence to its reserve model. While the Trust's investment performance will be the same with or without trustees designating permanent inflation proofing, permanent inflation proofing reduces flexibility to increase withdrawals beyond the Trust's spending policy. When this discipline is balanced with the 400% reserve model, the Trust can ensure a buffer exists to support spending to meet beneficiary needs should markets experience a severe decline.

As of December 31, 2020, fully inflation proofing the Trust Fund requires \$120,280,300. If earnings were to stay at the January 31, 2021 earnings level, nearly \$123MM would be available at fiscal-year end to meet the current inflation proofing needs.

Trust policy and past practice prioritizes inflation-proofing when sufficient reserves are available. As described above, the Trust can both meet its reserve target, which will prudently insulate the Trust from market volatility, and transfer available reserves to fully inflation-proof the Trust Fund. This action will provide confidence that the Trust is well positioned to serve beneficiaries now and into the future.