

MICHIGAN NATURAL RESOURCES TRUST FUND

BOARD OF TRUSTEES MEETING

Minutes of February 10, 2016

Lansing Community College West Campus, 5708 Cornerstone, Lansing
9:00 AM

The meeting of the Michigan Natural Resources Trust Fund (MNRTF) Board of Trustees commenced at 9:05 AM, Wednesday, February 10, 2016.

The following Board members were present:

Brad Canale
Sam Cummings
Steve Hamp
Erin McDonough
Dr. William Moritz (Director)

Also in attendance were various staff members of the Department of Natural Resources (DNR) and other interested parties.

I. ADOPTION OF MINUTES FOR MEETING OF DECEMBER 2, 2015.

Chairperson Canale called for the adoption of the minutes of the December 2, 2015 MNRTF Board meeting.

**MOVED BY MS. McDONOUGH, SUPPORTED BY DIRECTOR MORITZ, TO ADOPT THE MINUTES OF THE DECEMBER 2, 2015 MNRTF BOARD MEETING.
MOTION PASSED WITHOUT DISSENTING VOTE.**

II. ADOPTION OF AGENDA FOR MEETING OF FEBRUARY 10, 2016.

Chairperson Canale called for the adoption of the agenda for the February 10, 2016 MNRTF Board meeting.

**MOVED BY MR. CUMMINGS, SUPPORTED BY MS. McDONOUGH, TO ADOPT THE AGENDA FOR THE FEBRUARY 10, 2016 MNRTF BOARD MEETING.
MOTION PASSED WITHOUT DISSENTING VOTE.**

III. INTRODUCTIONS.

The Board members introduced themselves.

Mr. Steve DeBrabander, Manager, Grants Management Section, Finance and Operations Division, DNR, introduced himself and Grants Management staff: Mr. Jon Mayes (Unit Manager, MNRTF), Ms. Linda Harlow (Administrative Assistant to staff and Board), Mr. Mike

Chuff (MNRTF Financial Specialist), Ms. Amy Matisoff (Grant Coordinator), Ms. Tamara Jorkasky (Grant Coordinator), Mr. Chip Kosloski (Grant Coordinator), Ms. Merrie Carlock (Grant Coordinator), and Ms. Christie Bayus (Program Manager, LWCF/Marine Safety/Recreation Passport Programs).

Mr. DeBrabander also introduced Ms. Sharon Schafer, Chief of Finance and Operations Division, and Ms. Tina Stojakovich of DNR's Marketing and Outreach Division. Ms. Stojakovich does all the graphic work for the MNRTF.

IV. PUBLIC APPEARANCES.

Ms. Caitlin Donnelly, Land Protection Specialist, Little Traverse Conservancy

Ms. Caitlin Donnelly, Land Protection Specialist for Little Traverse Conservancy made comments on projects that the Conservancy is working on. She mentioned projects in Eveline Township in Charlevoix County and also a project in Emmet County. More information will be provided at future MNRTF meetings.

Michigan Department of Treasury Representatives – MNRTF Investments

Mr. Gregory Parker, Director of Investments; Mr. Woodrow Tyler, Senior Investment Manager; and Ms. Lan Chen, Treasury Investment Specialist, from the Bureau of Investments, Michigan Department of Treasury, provided a PowerPoint presentation to outline the asset allocation and investments for the MNRTF Program.

Mr. Parker outlined the current market conditions. Conditions were sluggish in 2015. Since the beginning of 2016, global stocks (U.S. S&P 500 Index, U.K. FTSE Index and Japan Nikkei Index) have been down; interest rates are down; and oil prices continue to decrease.

There is a global slowdown with China's growth slowing, Russia and Brazil in recessions, and the European market growth is slow. The U.S. recovery is slow in taking off, but the outlook is positive as there is low unemployment, housing and automobile sales are strong, improved State and Federal budgets, reduced energy costs and increased government spending.

The current 10-year Treasury yield is near historic lows. Between 2007 and 2008, the yield was about 5 percent. In 2015, rates dropped to 2.152 percent.

Mr. Parker outlined the long-term return and risk assumptions as identified by Aon Hewitt.

At this point, Ms. Chen outlined the current MNRTF portfolio. The MNRTF investment strategy outline is: **Liquidity** (ensure the availability of funds when needed to meet immediate and/or future requirements of the MNRTF), **Return** (managed in a manner to best meet long-term income needs of the MNRTF); and **Safety** (seek to contain the risks of principal loss).

Percentages of the MNRTF's current portfolio are invested as follows:

- 10.8% - cash equivalents
- 10.4% - U.S. government bonds
- 39.6% - corporate bonds
- 18.5% - equities
- 20.7% - alternatives

Most of the MNRTF's return is expected to come from investment income of approximately \$21.4 million (approximately 3%) over the next twelve months. These returns are in bonds, cash/commercial paper, equity dividends and alternative investments.

Ms. Chen outlined performance figures that have been identified as of December 31, 2015.

At this point, Mr. Cummings outlined the Innovative Funding Subcommittee's completed report (under Old Business). The report provides an assessment of innovative financing approaches and the MNRTF.

V. OLD BUSINESS.

Innovative Funding Subcommittee – Discussion of Completed Report

Mr. Cummings outlined the report that has been completed by the Innovative Funding Subcommittee. There has been a lot of discussion about the future of the MNRTF and how to meet its goals of conservation and outdoor recreation and how to best utilize its assets.

In 2015, the Innovative Funding Subcommittee was established to discuss how the MNRTF can achieve its goals. The subcommittee was led by Ms. Helen Taylor of The Nature Conservancy. Mr. Cummings stated that the recommendations of the subcommittee have not been discussed with staff from the Department of Treasury.

Mr. Cummings outlined the recommendations developed by the subcommittee. Some of the recommendations would require Board Policy action and others a Constitutional change. These recommendations are not necessarily for action at this time, but for discussion. At the Board's next meeting, there will be a more substantive discussion. Mr. Cummings would like to have a discussion with Treasury on a couple of the recommendations.

Recommendations are as follows:

1. **Adjust the current asset allocation of the MNRTF investments to increase the rate of return.**

Authority to Implement: The Department of Treasury has the responsibility of the investments.

2. **Adjust the spending rule from 2.5 percent to a minimum of 3.5 percent, or higher, dependent upon project priorities and if annual investment returns can support an increase.** A few years ago, the Board adjusted the percentage down to 2.5 percent when the MNRTF cap was reached (\$500 million). The goal of this was to increase the Stabilization/Growth Reserve to allow for “smoothing” in years where there was not a significant return.

Authority to Implement: This percentage is a Board Policy and can be adjusted at the Board’s discretion. Need to discuss with Department of Treasury for guidance. Recommendation 1 should be implemented first.

3. **Explore whether the MNRTF must maintain the acquisition or development “identity” on funds returned.** The Attorney General’s office was consulted and their informal review stated that revenues do not retain their identity of development or acquisition. The returned revenues, however, will have to have the formula applied once again as they are awarded.

Authority to Implement: The Michigan Constitution contains the authority to implement.

4. **The MNRTF Board should adopt the following principles in managing the MNRTF:**
 - **Rename all reserve and growth funds as “Stabilization Fund”;**
 - **Treat the MNRTF as an endowment to be maintained and utilized in perpetuity;**
 - **Anticipate market fluctuations by maintaining an appropriate investment portfolio with adequate resources to offset declines in income; and**
 - **Be prepared to act on large initiatives and statewide priorities.**

Authority to Implement: The MNRTF Board has the authority to adopt this recommendation.

5. **Bonds are a possible vehicle to fund statewide recreational projects and priorities.** Specific projects could use bond financing and the debt service could be paid for by the MNRTF.

Authority to Implement: The MNRTF Board has the authority to recommend bonding. The Michigan Strategic Fund has the authority to bond. The Michigan DNR would request a line item appropriation for debt service.

6. **Work with MNRTF staff and the Board to streamline administrative requirements, expand grant award frequency, and provide regional planning to communities to identify priority projects. Examples are:**

- **Explore legislative approval of a lump sum appropriation for high priority projects to be managed and executed by the MNRTF Board;**
- **Award projects in phases to span multiple years enabling large projects to be funded;**
- **Increase the number of application deadlines throughout the year;**
- **Manage annual cash-flow and projections to enable more than one grant approval cycle;**
- **Increase the number of supplemental bills annually submitted for legislative approval to increase cash flow to projects, enabling timely project development;**
- **Streamline administrative functions to:**
 - o **Process a greater volume of grant applications; and**
 - o **Enable staff to facilitate regional projects to enhance collaboration, leverage MNRTF resources, and identify additional priority initiatives. The regional role MNRTF staff might play could be aligned with the Administration's prosperity regions, strengthening integration with multiple state department strategies.**

Authority to Implement: The MNRTF Board and DNR have the authority to implement administrative process changes.

7. **Continue to grow the MNRTF to maintain purchasing power, index to inflation, and dedicate mineral revenue to natural resources for the future.** This would require an amendment to the Michigan Constitution, which is not recommended at this time; however, if in the future there is an initiative to amend the Constitution, that consideration be given to indexing the MNRTF to inflation, and seek permanent dedication of mineral revenues to natural resource protection. Under current Constitutional language, once the State Park Endowment Fund reaches \$800 million, the mineral revenue is to be deposited as provided by law. Revision of this language to dedicate those revenues to natural resources for the future should be pursued before the end of 2018.

Authority to Implement: Constitutional Amendment.

Mr. DeBrabander advised the audience that the subcommittee's final summary recommendations report is located on the DNR's website. Mr. Cummings asked that this report be sent to staff at the Department of Treasury. Mr. DeBrabander will take care of this.

Ms. McDonough asked, as to large projects, if there was a plan to actually communicate with communities to get a sense of how they feel about this. Mr. DeBrabander responded that over the next two months the Board will go through the report and evaluate the recommendations and we will have a more robust discussion at the April Board meeting. Whether there will be action then will be up to the Board.

Mr. Cummings added that there may be parts of the report that will be adopted and others that are not. Some recommendations may be modified.

Ms. McDonough further stated that recreation grant workshops are being conducted now. She feels we need to get some additional feedback, as from past conversations there are some concerns about the MNRTF Board moving towards allocating most of the funds for large projects. Mr. DeBrabander responded that this is on the web, and our customers can provide comments or suggestions regarding the recommendations to the Board or staff.

Mr. Cummings added that he feels the intent is to find a way to fund large projects and at the same time continue to provide the same level of funding for smaller projects.

Chairperson Canale stated that he respected the partnership of the subcommittee members. This document is a good basis for what can be discussed at the April Board meeting. Mr. Hamp concurred; most of the recommendations are allowable at the MNRTF Board level.

Michigan Department of Treasury Presentation (continued)

At this point, Mr. Parker continued with the Department of Treasury presentation by outlining the proposed asset allocation changes for the MNRTF – Liquidity, Return and Safety.

Liquidity – current project commitments are estimated to be around \$75 million. The recommendation is to invest in a laddered portfolio of government-related bonds to meet commitments for the next four to five years.

Future operating requirements are estimated at approximately \$80 million over the next three years. The recommendation is to invest in a laddered portfolio of government-related bonds with maturities scheduled to meet the cash flow needs over the next three years.

Return – additional asset classes will improve returns and increase diversification--high yield bonds (add return); hedge fund-of-funds (increase diversification); alternative investments (add return—primarily credit-related investments with current yield); and private equity (add return—activist public equity managers with private equity return expectations or private equity secondaries).

The proposed portfolio steps are as follows:

1. **Portfolio Step 1 - Improve returns of existing portfolio while providing funding for current and future project commitments.** The current allocation has an expected return of 4.5% with risk of 7%. This step will allocate a portion of bonds to current project commitments and future operating requirements of \$80 million over the next three years. The expected return is 5.7% with a 9.0% risk.
2. **Portfolio Step 2 - Improve returns of proposed portfolio 1 by increasing allocation to public equity and high yield and trimming exposure to government-related bonds.** This step will have an expected return of 6.0% with risk of 10.2%.

Some recent changes are:

- December 2015 – added Prudential High Yield bond fund. It is expected to have returns similar to equity, but with significantly less risk.
- January 20, 2016 – added to equities to bring the full weight to 20% of the total portfolio.

In conclusion, action to be taken over the next six months includes:

Portfolio 1:

- Build ladder portfolio of safe government bonds to fund: Current MNRTF project commitments and future operating requirements of \$80 million.
- Research and meet with managers across new asset classes: high yield, hedge fund-of-funds, alternatives and private equity.

Portfolio 2:

- Over three years, fund future requirements and reallocate assets to Portfolio 2.

A chart was outlined of annual total returns for key asset classes from 1995-2014.

MOVED BY MR. CUMMINGS, SUPPORTED BY MR. HAMP, TO ACCEPT THE DEPARTMENT OF TREASURY'S OUTLINED PLAN FOR ASSET ALLOCATION AND INVESTMENTS FOR THE MNRTF PROGRAM. MOTION PASSED WITHOUT DISSENTING VOTE.

MOVED BY DIRECTOR MORITZ, SUPPORTED BY MR. HAMP, TO ACCEPT THE INNOVATIVE FINANCE SUBCOMMITTEE'S FINAL SUMMARY RECOMMENDATIONS REPORT. THE REPORT WILL BE DISCUSSED FURTHER AT THE BOARD'S APRIL 13, 2016 MEETING AND MODIFICATIONS COULD BE MADE AT THAT TIME. MOTION PASSED WITHOUT DISSENTING VOTE.

VI. NEW BUSINESS.

Update on MNRTF Staff Activities

Mr. DeBrabander outlined various MNRTF staff activities:

- Staff has been busy conducting recreation grant workshops around the state. Workshops were completed in Baraga, Ann Arbor, Escanaba, Lansing, Frankenmuth, St. Ignace, West Branch, Southfield and Grand Rapids. Staff received very good reviews. A recreation grants workshop will be conducted at the MParks (Michigan Recreation and Park Association) Conference in Traverse City on February 17.
- Director Moritz and Ms. McDonough will be participating in a MNRTF Round Table discussion at the MParks Conference.
- Staff continues work on the MiRecGrants system. Amy Matisoff is the lead on the system. About 85 percent of the system has been completed. This will be the third year that recreation grant applications for MNRTF, Land and Water Conservation Fund and Recreation Passport grant programs have been submitted through MiRecGrants.
- The Post-Completion Self-Certification inspection process has now been completed. All 83 counties have received inspection reports. Linda Harlow has been working on the inspection process.
- Interviews for Linda Harlow's position will be conducted Thursday and Friday of this week.
- The 2015 MNRTF Annual Report has been completed and the Board has received a copy today. This has also been posted on the web.
- The National Association of State Outdoor Recreation Liaison Officers (NASORLO) annual conference will be held in Detroit in September of this year. Representatives meet annually to discuss with the federal Land and Water Conservation Fund Program.
- Grants Management Section now has a 12th grant program – the Clean Vessel Act grant program. Kammy Frayre will be the program manager for this grant program. She also is the program manager for the Invasive Species grant program and is the conversions officer. The Clean Vessel Act grant program is federally funded and funds pump out stations at marinas.
- There has been no movement of the MNRTF Bill which contains the 2015 projects.

- 2016 is the 40th anniversary of the MNRTF Program. A number of activities are being planned. Merrie Carlock is taking the lead on planning activities, with Tina Stojakovich from Marketing and Outreach Division assisting.

At this point, Ms. Carlock outlined aspects of 40th anniversary plans. The 40th anniversary logo has been announced today. The logo will be on emails and other items. The plan is to have anniversary celebrations in conjunction with the June (Onkama), August (Port Huron) and October (Lansing) Board meetings. The October celebration is being proposed as more formal (evening event the day before the October meeting). The DNR has been partners with the Michigan Oil and Gas Association, Michigan Recreation and Park Association (now MParks), and Michigan United Conservation Clubs. Unlike the last anniversary celebrations, we now have web access and Facebook.

Ms. Stojakovich displayed the graphic for the 40th anniversary. There will be showcasing of articles and programs that highlight the MNRTF. There will be a press release and other messaging tools used to advertise the anniversary celebrations.

Conversion Update

Mr. DeBrabander updated the Board on the status of conversion efforts involved with Riverside Park in the City of Detroit. This is the proposed site where Manuel (Matty) Moroun wants to build a new bridge. Riverside Park received funding under the Land and Water Conservation Fund (LWCF) and the MNRTF. This would involve a conversion of the site to a non-recreational use. As of this date, Grants Management has not received a formal conversion request from the City of Detroit.

Mr. DeBrabander and Ms. Bayus (Program Manager for the LWCF Program) had a meeting a couple weeks ago and met with 13 City of Detroit officials and talked about the process, conversion and mitigation properties. Two months ago, the city submitted their environmental assessment for review. Both DNR and Michigan Department of Transportation staff have been reviewing the environmental assessment. It is anticipated that an application for conversion will be submitted before the April Board meeting.

VII. STATUS REPORTS.

DNR Real Estate Report

Mr. Jon Mayes advised the Board that there were two new DNR acquisitions that were taken to then Director Creagh for approval. These parcels are: Weronko Parcel (Lake County) and Wigwam Duck Club Parcel (Arenac County).

Completed MNRTF Projects Report

No discussion.

MNRTF Financial Report

Ms. Schafer outlined the MNRTF financial report. The format of the report has been changed and she welcomed any feedback from the Board on its style.

Ms. Schafer stated that the 2016 beginning investment balance was \$578.7 million which is slightly lower than last year. The reason for this is that the Board took action last December to increase spending for additional projects (based on 5% spending). She pointed out that the new report format is not broken out between the Stabilization Fund and Growth Reserve.

The investment income is estimated at \$31.8 million. This is based on a 5.5% return. This probably will have to be revisited based on the information that the Department of Treasury provided. Staff will continue to be in contact with Treasury throughout the year for any adjustments. The balance of other income was \$150,000.

Based on conversation with the Attorney General's office, we no longer need to track the lapses as to acquisition or development. The balance for lapses and withdrawals was \$567,589. This figure could change over the year.

Based on an investment income distribution of 2.5%, the amount available for 2016 projects is estimated to be \$11.6 million (\$7.8 million for acquisition and \$3.7 million for development).

Chairperson Canale asked what the current amount was for approved grants that have not yet been distributed. Ms. Schafer will find out and let Chairperson Canale know.

Director Moritz asked if the Board went with 3.5%, would that affect the projections or would that be effective in 2017.

MNRTF Land Consolidation and Line Item Department Projects

No discussion.

VIII. OTHER MATTERS AS ARE PROPERLY BROUGHT BEFORE THE BOARD.

None.

IX. ANNOUNCEMENTS.

The next meeting of the Michigan Natural Resources Trust Fund Board is scheduled for 9:00 AM, Wednesday, April 13, 2016, Lansing Center, Governor's Room, 333 E. Michigan Avenue, Lansing, Michigan.

X. ADJOURNMENT.

**MOVED BY MS. McDONOUGH, SUPPORTED BY MR. HAMP TO ADJOURN
THE MEETING. MOTION PASSED WITHOUT DISSENTING VOTE.**

The meeting was adjourned at 10:40 AM.

Brad Canale, Chairperson
Michigan Natural Resources Trust Fund
Board of Trustees

Steven J. DeBrabander, Manager
Grants Management Section
Finance and Operations Division

DATE