

MINUTES

Committee on Administration and Finance

December 8, 2011

John Murphy Conference Room

Minnesota Medical Association

1300 Godward Street NE, Suite 2500

Minneapolis, MN 55413

Members Present

David Westgard, MD
Richard Simmons, MD
Michael Ainslie, MD
James Dehen, MD
Noel Peterson, MD
Joel Greenwald, MD
Carolyn McKay, MD, MPH
Daniel Maddox, MD

Members Absent

Peter Dehnel, MD
Charles Terzian, MD
David Sproat, MD

Guests Present

Jerry Prostrollo-Midwest Capital Mgmt.
Todd Harmsen-RBC Capital Mgmt.
Mike Dickson,-RBC Capital Mgmt.

Staff Present

Robert Meiches, MD
George Lohmer
Jon Stensland

I. Call to Order/Approval of Minutes

The following motion was made, seconded and passed:

Motion: that the minutes of the November 3, 2011 meeting be adopted.

II. Financial Statement Review

Jon Stensland reviewed with the Committee the October 2011 MMA financials.

The following motion was made, seconded and passed:

Motion: that the September 2011 financials be accepted as presented.

III. MMA IA Manager Review

Jon Stensland introduced Todd Harmsen and Mike Dickson from RBC Capital Group and Jerry Prostrollo, Midwest Capital Management. RBC has been retained as the investment management consultant for the MMA IA. Jerry Prostrollo has been retained, among other responsibilities, to evaluate the performance of the RBC.

At the last meeting the Committee directed that an overall assessment of the performance of the MMA IA management be discussed at this meeting. The representatives from RBC presented their review of the performance of the account and subsequently left the room for committee discussion. It was determined that the variances in performance were satisfactorily explained. The Committee was quite comfortable in continuing to use this group as the investment management consultants. After this discussion Jerry Prostrollo left the room. The Committee also discussed Jerry's role as the financial adviser for the Committee. It is understood that Jerry's role is to:

- assess the performance of the Investment Management Consultant and to recommend changes in the consultants when appropriate
- manage the investment management review process as outlined in the investment policy
- monitor and recommend changes in the investment policy
- communicate to the committee investment performance, recommendations and investment manager and investment management consultant performance

In assessing the investment management consultant performance Jerry is asked to translate the RBC "techno-speak" into understandable language, explain RBC decisions and rationale to assess RBC performance against the MMA IA investment policy. It was also recommended that the RBC Capital be asked for an annual review performance.

IV. MMA 2012 Budget Overview

George Lohmer reviewed with the Committee the status of the MMA 2012 budget. From an operating account perspective the budget is basically balanced (i.e., -\$5,000 deficit). However the budget does not reflect the implementation of the priorities of the MMA strategic plan, primarily driven by the identification, actions and funding of strategic initiatives. It is proposed that the assets in the MMA IA might be considered as a source of funds for strategic initiatives along with other already identified uses for the MMA IA. This language is reflected in a revision on the MMA IA Investment Policy (Exhibit A).

A second issue was also discussed by the Committee. In the MMA's financial management report a section has been developed (Adjustment Section) which allows for "off-sets" of expenses and other items from the MMA Operating account. The Committee directed staff to develop a policy on when this section should be used. This financial policy was outlined in Exhibit A.

The following motion was made, seconded and passed:

Motion: that the proposed motions contained in the document titled "MMA Financial Policies-Guidelines on Expenditures to be Recognized in the Adjustment Section of MMA's Financial Management Reports" be adopted and forwarded to the MMA board for approval.

V. Next Meeting and Adjournment

The next meeting of the committee is January 12, 2012.

The following motion was made, seconded and passed:

Motion: that the meeting be adjourned.

DRAFT

MMA Financial Policies

Guidelines on Expenditures to be Recognized in the Adjustment Section Of MMA's Financial Management Reports

The purpose of this document is to identify a financial policy to provide guidance on the types of expenditures that may be recognized in the Adjustment section of MMA's Financial Management Reports.

The following motions are presented for approval:

Motion: That the MMA IA Investment Policy be revised to add "To provide interim funding for Strategic Initiatives" as an additional purpose for the use of the assets of the MMA IA.

Motion: That the MMA adopt the proposed "Adjustment Section Policy" and the accompanying four Policy Statements.

Background

On a monthly basis the MMA produces a set of financial management reports. Two primary reports are produced: MMA Balance Sheet and MMA Income Statement. These two financial statements vary from generally accepted accounting procedures (GAAP) in a number of ways so as to improve their use as a financial management reports. Some of the major variances include:

- not incorporating the MMAF into MMA's financials
- development of a special section for investment income. (This separate section displays investment results isolated from operating results.)
- development of a special section for board approved exceptions. This section is titled "Adjustments".

At year end the MMA utilizes an independent auditor to reformat its financials according to GAAP standards.

The MMA board has determined that certain expenditures can be exempted from the operating account. **The general rationale for this exemption is that these are exceptional expenses appropriately funded out of the MMA's "savings" account (i.e., MMA IA) and not funded out of operations which would cause additional cuts to be made elsewhere in the MMA operating budget.** In addition, the board has also recognized that the current value of certain equity investments can also be recognized as an adjustment to operating results. Since 2003 the following items have been included in the Adjustment section of MMA's financial management reports:

Adjustment Section Expenses Since 2003

Item #	Item Description	Estimated Amount	Financing Source ¹
1	Contributions to Minnesota Community Measurement	\$300,000	Operations (Approx. \$40-\$45,000 /year over the last 7 years)
2	Purchase of ClearVantage, the MMA database platform	\$173,500	MMA IA (Amortized in Operating Account)
3	Software upgrade for the accounting department	\$12,000	MMA IA (Amortized in Operating Account)
4	Costs associated with the estimated dues revenue loss for the implementation of the Multi-Year Membership Program	\$210,000	MMA IA (Funded over 3 years at a rate of \$105,000, \$70,000 and \$35,000)
5	Cost of the MMA's move into 1300 Godward Street site	\$67,300	MMA IA (Amortized in Operating Account)
6	Cost of the workstations and related items for 1300 Godward Street site	\$167,000	MMA IA (Amortized in Operating Account)
7	Website Redesign	\$110,000	MMA IA (Amortized in Operating Account)
8	Budgeting System Upgrade	\$30,000	MMA IA (Amortized in Operating Account)
9	Health Care Reform Activities	\$50,000	MMA IA (Expensed in Operating Account)
10	CEO Transition Expenses	\$130,000	MMA IA (Amortized in Operating Account)
11	Non-Equity Investments in MCC	\$49,000	Operations (Expensed in Operating Account)
12	Equity Investment in MCC	\$150,000	MMA IA (Equity Investment-MMA Balance Sheet Item)
13	Sabbatical Expenses	\$35,000	MMA IA (Expensed in Operating Account)
14	LTI	\$23,000	MMA IA (Expensed in Operating Account)
15	Current value of equity investments in MMBR (Member Advantage)	NA	(Equity Investment-MMA Balance Sheet Item)
16	Current value of equity investment in MMJSO	NA	(Equity Investment-MMA Balance Sheet Item)

Equity investments in related organizations have also been recognized in the Adjustment Section. Both the MMJSO and MMBR (now known as Member Advantage) are reflected in the Adjustment section. The primary rationale for their inclusions in the Adjustment section has been that their activities would have been reflected directly in MMA operations if the organizations had not been separately incorporated. Member Advantage is jointly owned by the MMA and TCMS. The primary sponsors of the MMJSO are the MMA and TCMS².

MMA Investment Account (MMA IA)³

¹ Use of the term "Amortized" indicates that the expense was recognized over a number of years, while the use of the term "Expensed" indicates that the expense was recognized all in one year.

² Other participating organizations include MMAF, Member Advantage and MCC.

³ MMA IA Investment Policy (IP) is attached. The IP also provides for the transfer of 1% of the value of the MMA IA (based on a 5 year average) to operations as a CEO Discretionary Account.

The Minnesota Medical Association has set aside some of its resources into a long-term investment account, called the Minnesota Medical Association Investment Account (MMA IA) whose assets may be used for the following reasons:

- To provide resources during short-term (e.g., 1-2 years) adverse financial periods
- To take advantage of unique investment opportunities
- To provide contributions to un-related organizations
- To provide resources for major infrastructure investments
- To provide professional development resources for MMA staff

The current value of the MMA IA as of 11/16/2011 \$5,853,783 (after a transfer of \$300,000 of working capital into the operating account which will be replaced as dues revenue allows).

In almost every case the expenses recognized in the Adjustment section were funded by the MMA IA or were organizations in which the MMA had equity investments with related organizations.

Proposed Adjustment Section Policy

Policy Statement 1-The purpose of the Adjustment Section is to:

- reverse the expense of selected expenditures funded by the MMA IA consistent with the purposes of the MMA IA Investment Policy or
- recognize the ongoing value of the equity investments in related organizations

Policy Statement 2-All transactions displayed in the Adjustment section will be approved by the MMA board of trustees as recommended by the Committee on Administration and Finance. The MMA board of trustees may make an exception to this policy and include additional items based on a specific mandate.

Policy Statement 3-All Adjustment section transactions, exclusive of equity investments in related organizations, must meet the following criteria:

1. To take advantage of unique investment opportunities
2. To provide interim funding for Strategic Initiatives⁴
3. To provide contributions to un-related organizations
4. To provide resources for major infrastructure investments
5. To provide professional development resources for MMA staff

Policy Statement 4-Equity investments may be reflected in the Adjustment section if:

- Funded through a MMA IA investment and
- A MMA subsidiary (i.e., MMA share of ownership is 50% or greater) and
- The MMA would be expected to provide the services offered by the subsidiary if the subsidiary did not exist.

If these criteria were applied to past transactions in the Adjustment section, the following expenditures would have been recognized as indicated:

⁴ Item 2 should be added as an additional purpose of the MMA IA. This issue will be discussed by the Committee on Administration and Finance.

Item #	Item Description	Meets "Adjustment" section criteria/ Criteria Met
1	Contributions to Minnesota Community Measurement	Yes/3
2	Purchase of ClearVantage, the MMA database platform	Yes/4
3	Software upgrade for the accounting department	Yes/4
4	Costs associated with the estimated dues revenue loss for the implementation of the Multi-Year Membership Program	Yes/2
5	Cost of the MMA's move into 1300 Godward Street site	Yes/4
6	Cost of the workstations and related items for 1300 Godward Street site	Yes/4
7	Website Redesign	Yes/4
8	Budgeting System Upgrade	Yes/4
9	Health Care Reform Activities	Yes/2
10	CEO Transition Expenses	No
11	Non-Equity Investments in MCC	Yes/1
12	Equity Investment in MCC	No-Does not meet definition of a MMA subsidiary
13	Sabbatical Expenses	Yes/5
14	LTI	?/If "Yes/2"
15	Current value of equity investments in MMBR (Member Advantage)	Yes- Meets definition of a MMA subsidiary
16	Current value of equity investment in MMJSO	Yes- Meets definition of a MMA subsidiary. Value zeros-out at year end.

MMA Investment Account (MMA IA) Investment Guidelines and Spending Policy

This document is divided into three major sections:

1. **Purpose of the MMA IA**-This section describes the reason for the existence and the major purposes of the MMA Investment Account and the overall investment philosophy.
2. **Investment Guidelines**-This section describes how the assets are to be invested, the size of the account, any investment restrictions and financial/fiduciary oversight protocols to assure prudent management of the investments.
3. **Spending Policy**-The section describes how the assets in the MMA IA will be spent addressing budgeted and un-budgeted uses of the assets in the MMA IA, how assets will be transferred and the use of these assets to provide contributions to un-related organizations.

Purpose of MMA IA

The Minnesota Medical Association has set aside some of its assets into a long-term investment account, called the Minnesota Medical Association Investment Account (MMA IA) whose assets may be used for the following reasons:

- To provide resources during short-term (e.g., 1-2 years) adverse financial periods
- To provide interim funding for Strategic Initiatives
- To take advantage of unique investment opportunities
- To provide contributions to un-related organizations
- To provide resources for major infrastructure investments
- To provide professional development resources for MMA staff

MMA IA assets are invested according to the investment guidelines cited below. These guidelines are approved by the MMA Board of Trustees, used as an oversight tool by the Committee on Administration and Finance and as guiding principles by MMA staff and investment advisers hired by the Committee.

The members of the MMA, through their dues commitments and purchases of services, have made the MMA IA possible. The MMA is, in fact, a steward of the funds in the MMA IA. The MMA IA will be invested in a 60% Equity, 40% Fixed Income Allocation. The goal of this investment philosophy would mean that the funds will be invested in such a way that the account should lose less than average (e.g. as measured by the S&P 500 or other selected broad market index) in a down market but would not be expected to outperform this measurement in an up market (i.e., less volatility). The MMA IA's assets will be allocated across a variety of asset classes in such a way as to accomplish this investment return in two major ways:

The asset allocation model currently provides rebalancing guidance between equity and fixed income (equity/bond allocations may range from 50%/50% to 70%/30%). Rebalancing also applies to ranges around the various sub-asset classes (between large growth, large value, small-mid cap, and international equities). By implementing ranges around long-term strategic targets the committee is better able to monitor the efficiency of the asset allocation, thereby helping to mitigate volatility.

The target ranges are as follows:

Broad Asset Class / Peer Group	Lower Limit	Strategic Target	Upper Limit
Fixed Income Intermediate Fixed Income	30.0	40.0	50.0
Domestic Large Cap Value	10.0	17.0	25.0
Domestic Large Growth	10.0	13.0	25.0
Small-Mid Cap Equity	5.0	15.0	20.0
International Equity	10.0	15.0	30.0
Real Estate (REITs)	0.0	0.0	10.0

As movement in an asset class approached its upper or lower limits the committee will discuss how funds should be re-allocated.

- Asset class selection (e.g., large capitalization growth stocks, fixed income)
- Asset class expense minimization (Much of the investment cost is driven by the need to be sensitive to restrictions imposed by the MMA House of Delegates on the type of allowable investments (i.e., no investment in companies the produce tobacco products))

Investment returns, for each manager, will aim to be equal to or greater than the appropriate benchmark for that manager.

Size/Contributions/Withdrawals to/from the MMA IA

The corpus of the MMA IA is to be between 12 and 24 months of operating expenses of the MMA Operating Account with an average of 18 months of MMA operating expenses as a target. The American Society of Association Executives (ASAE) recommends that associations maintain a minimum of 6-9 months reserve.

If the MMA IA's corpus falls below 12 months of operating expenses, the MMA should implement a schedule to move the corpus up to 18 months of operating expenses over a 2-5 year period. If the MMA IA's corpus exceeds 24 months of operating revenue the MMA should consider implementing a schedule of transfers to operations or the Minnesota Medical Association Foundation which would over a period of 2-5 years move the corpus below 24 months and no less than 18 months.

Transfers from the MMA IA into the MMA Operating Account will be based on the MMA IA Spending Policy.

Investment Guidelines

Investment Management Guidelines

The Committee on Administration and Finance will use the following guidelines to evaluate the performance of selected investment managers.

- Based on long term market trends, a model portfolio will be used as an asset allocation model reflecting both the risk profile of the account and expected returns. Using a 60% equity/40% fixed income model portfolio it would be expected that the MMA IA would see an overall rate of return of approx. 8%. The overall MMAIA portfolio will be structured as a 60% Equity, 40% Fixed Income Allocation. The equity/bond allocations may range from 50%/50% to 70%/30%.
- Investments will be limited to long purchases of equities, fixed income, cash and cash equivalents, and exchange traded funds ((ETFs)
- Investments will exclude:
 - Short sales
 - Puts, calls, and other options
 - Commodity contracts
 - Non-negotiable and non-marketable securities
 - Margin purchases and other uses of borrowed funds
 - Companies that produce tobacco products⁵
 - Hedge techniques and derivatives.
 - Non-investment grade fixed income securities
- Only investments that can be purchased/sold/traded through multiple, independent financial sources will be used
- Only investments that report to generally acceptable third party reporting services will be used.
- Fixed return investments (Bonds) will be invested in investment grade^[1], securities.
- Equity investments (Stocks) will reflect an asset allocation model including a mix of asset classes.

Investment performance will be measured on an absolute and relative basis. The Committee on Administration and Finance will determine, for each investment manager, the indices, peer group and benchmark performance ratings used for performance evaluation. The indices selected for each manager will depend on the style of the selected manager.

These guidelines are subject to exception, recommended by the Committee on Administration and Finance and approved by the Board of Trustees.

Responsibilities of the MMA Staff and the Committee on Administration and Finance for the Management of Fund and of the Investment Managers

The MMA Committee on Administration and Finance exercises delegated oversight for the management of the MMA Investment Account (MMAIA) from the MMA Board of Trustees. This oversight authority is based on Investment Guidelines approved by the MMA Board of Trustees.

⁵ The MMA IA is prohibited from making investments in companies that produce tobacco products. MMA IA's investment managers shall monitor all investments for direct or indirect (e.g., within a mutual fund or ETF) ownership of companies that produce tobacco products at the time of the purchase of the investment or may be acquired after an initial investment purchase. If direct or indirect ownership is found the MMA IA will divest itself of these investments as soon as feasible and reinvest these funds according to the MMA IA Investment Policy. Any divestment made under these circumstances will be reported to the MMA CFO immediately

[1] S&P: BBB- or higher; Moody's: Baa3 or higher.

The Committee on Administration and Finance has developed Investment Guidelines and timetables that it will use to carry out its fiduciary responsibilities for the prudent management of the MMAIA.

MMA Staff Management Responsibilities

- Monitor cash levels in all accounts to assure sufficient cash for operating needs and for other expected distributions.
- Review monthly and quarterly statements for deposit/withdrawal confirmations
- Monitor quarterly performance information provided by Investment Advisor and Brokerage Agency
- Provide timely reports to the Committee on Administration and Finance and Chairperson, as appropriate, on the performance of fund managers
- Monitor performance of Investment Advisor

Quarterly Review

On a quarterly basis the Committee on Administration and Finance, the Chairperson or designee(s) will review reports provided by the Investment Adviser and Brokerage Agency.

Annual Review

At least on an annual basis the Committee on Administration and Finance will:

- Determine the number of investment accounts.
- Determine the overall asset allocation of the accounts.
- Evaluate the performance of each investment account based on the criteria listed in the “Investment Manager Guidelines”

Determine, for newly selected investment accounts, the commonly accepted indices and peer group and benchmark performance ratings, to be used to evaluate the investment manager.

Triennial Review

At least on a triennial basis the Committee on Administration and Finance will:

- Review Investment Guidelines
- Determine whether the funds should be individually managed or whether mutual funds should be utilized for part or all of the investments
- Determine the number of investment managers necessary for sufficient diversity and asset allocation
- Determine whether each fund is being managed in the most cost-effective manner

Spending Policy

The Spending Policy describes how the transfers from the MMA IA will be made.

- 1% Spending Guideline
- Other Transfers

The concept of a Spending Policy was developed by the Ford Foundation, in a ground-breaking study in 1968. Their study, aimed originally at family foundations and endowments, recommended spending 5% of an endowment's corpus each year based on three year moving average. In legislation at about the same time, the US Congress developed a test that required private foundations to make annual expenditures to maintain their current tax status.

A Spending Policy is a written policy that authorizes the expenditure/transfer of a certain percentage of an investment account, every year, to support the operations of an organization.^[3] There are several reasons for a Spending Policy including:

- Application of a disciplined and reasoned approach to moving money from an investment account to operations
- Making sure that expenditures/transfers are done on a predictable consistent basis
- Insuring intergenerational (or in the MMA's case, member) equity in assuring future members of having access to resources that current members have

1% Spending Guideline

The MMA's Spending Policy, will, on an annual basis, budget and transfer up to 1% of the value of the MMA IA into operations to be reflected in the CEO Discretionary Account. The Discretionary Account will be used by the MMA CEO to fund unexpected/unbudgeted expenditures and to staff professional development. Both of these expenditures may also be supplemented by adding additional dollars from the Operating Account.

To assure a more predictable level of expenditure/transfer of funds a 5-year rolling average based on the 12/31 value of the MMA IA. For example, to determine the amount of the expenditure/transfer for the 2007 budget, the following calculation would be performed:

Year	MMA Balance as of 12/31
1	\$6,803,809
2	\$5,749,930
3	\$6,081,651
4	\$6,112,878
5	\$5,773,992
5 Year Average	\$6,104,453
1% Value	\$61,045

The CEO Discretionary Account (which is funded by the Spending Account and by operations) is under the supervision of the CEO and allows the MMA flexibility to address unique funding opportunities, contributions to un-related organizations or a variety of unexpected expenses. The expenditure approval process is based on the proposed size of the expenditure. The following table displays, by size of expenditure, the approval process:

^[3] Spending Policy-Commonfund (www.commonfund.org/commonfund/investor+services/spending_policy)

Size of Expenditure	Approval Process
\$0-\$1,000	CEO approval; discussion with Board Chair and/or Treasurer concurrent with or after authorization
\$1,000-\$10,000	CEO approval based on discussion with Board Chair and Treasurer previous to authorization
More than \$10,000	CEO recommended based on approval by Executive Committee and/or Board

On a semi-annual basis expenditures/transfers out of the Discretionary Account will be reported to the Committee on Administration and Finance. The actual expenditure made with funds from the CEO Discretionary Account will be reflected in the appropriate project code and line item.

Other Transfers

From time-to-time the MMA finds it necessary to make large expenditures/transfers (e.g., greater than \$50,000). These expenditures/transfers may be budgeted or unbudgeted, but most are budgeted. For example, large budgeted expenditures/transfers that were financed by the MMA IA included the MMA's contribution to the Community Measurement Project or the MMA's purchase of a major upgrade of its data system. An example of a large unbudgeted expenditure/transfer that might require the use of the MMA IA would be the first year loss of dues revenue from a large medical group.

Almost any of the purposes of the MMA IA, could result in a need to transfer MMA IA assets to operations. Because of this large and sometimes unpredictable need, the Spending Policy limit of 1% was imposed to allow for the build-up of assets for larger expenditures/transfers while still allowing for real growth in the MMA IA.

When MMA IA Other Transfers are contemplated to be made, the MMA CEO will consult with the MMA Board Chair and Treasurer to determine the process for discussion and approval. The timeframe for making a decision regarding the expenditure/transfer, the size of the expenditure/transfer and policy implications of the expenditure/transfer will all be used as criteria to determine the process to be used for decision.

Guidelines for Contributions to Un-Related Organizations

From time to time the MMA provides contributions to outside organizations. The MMA may support a limited number of organizations and activities that best meet the following criteria:

- The contribution will be used for a project that is a direct benefit to the practice of medicine in the state of Minnesota.
- The contribution will be used for a project that contributes to the accomplishment of MMA mission or goals.
- The contribution will be for a single year.
- There will be no contributions for medical research.

The MMA Board of Trustees can make exceptions to these contribution criteria and award contributions on an “as needed” basis.

DRAFT