



TREASURER OF THE STATE OF LOUISIANA

# Medicaid Trust Fund for the Elderly

Statement of Investment and Cash Management  
Policy and Procedures

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**Statement of Investment and Cash Management  
Policy and Procedures for the  
MEDICAID TRUST FUND FOR THE ELDERLY**

**I. PREAMBLE**

The Medicaid Trust Fund was established under La. R.S. 46:2691 as a permanent trust funded through the proceeds of the intergovernmental transfer program. Monies in the fund may be used as the source of state matching funds for Medicaid funds to make enhanced payments to local government-owned health care facilities.

The principal in the fund shall not be subject to appropriation, except to provide for:

- A. The re-basing of nursing homes in accordance with the approved state Medicaid plan.
- B. The development and funding of a case mix reimbursement system for the Medicaid nursing home program.
- C. The payment of all costs of local governments for their participation in the intergovernmental transfer program.
- D. The enhanced payment to any local government-owned health care facilities or health care programs in amounts as required by written agreements between the secretary and the local governments which are recommended by the Intergovernmental Transfer Subcommittee created by and established in R.S. 46:2692 and approved by the governor and the Joint Legislative Committee on the Budget.
- E. The reimbursement of the Department of Health and Hospitals for costs incurred in preparing the application for and implementing the intergovernmental transfer program.

Appropriations may only come from earnings on investment from the fund. Re-basing in accordance with the approved state Medicaid plan may come from the principal in the trust, but shall be limited to earnings on investment from the fund. The earnings may be appropriated each fiscal year for services of the state Medicaid program in the following order of priority:

- A. For providing for a wage enhancement for direct care personnel working in Medicaid certified nursing homes in accordance with a plan established by the Department of Health and Hospitals and representatives of the nursing facility industry. The plan shall provide for a direct pass-through

sure that the home rate is adjusted to reflect the full costs of such wage enhancement.

- B. For appropriations solely and exclusively for services of the state Medicaid program that are subject to federal financial participation in matching funds.

In establishing investment goals and policies for the Medicaid Trust Fund, the state treasurer shall consult no less frequently than semiannually with the secretary of the Department of Health and Hospitals as to the anticipated cash withdrawals from the fund during the next twelve months.

The State Treasurer has the authority to contract for the outside management of the Medicaid Trust Fund assets. All appropriations made to, or upon the request of, the state treasurer, related to the management of the fund shall be subject to review of the Intergovernmental Transfer Subcommittee.

The State Treasurer shall report the status of the fund at least quarterly to the secretary of the Department of Health and Hospitals and the Intergovernmental Transfer Subcommittee.

On or before November first of each year, the State Treasurer shall prepare and submit to the secretary of the Department of Health and Hospitals a report on the performance of the fund during the prior fiscal year. The State Treasurer shall also submit a copy of the report to the Joint Legislative Committee on the Budget and to the House Committee on Health and the Senate Committee on Health and Welfare.

This document sets forth the following:

- A. The investment policies and objectives which the State Treasurer deems to be appropriate for the prudent investment and strategic planning of the Medicaid Trust Fund for the Elderly.
- B. The investment policies and objectives, and the selection of investment managers and performance criteria for investment managers.
- C. A guide used by the Treasurer and advisory committee or group formed by the Treasurer for the ongoing supervision of the investment program for the Medicaid Trust Fund for the Elderly Fund to ensure that the assets remain invested in accordance with this document.
- D. Accounting and reporting guidelines for the purposes of measuring the performance of the Medicaid Trust Fund for the Elderly.

## **II. RESPONSIBILITY & MANAGEMENT**

The State Treasurer may promulgate rules for the overall investment of the Medicaid Trust Fund and shall employ an investment staff to manage the assets and to ensure that the fund is invested in accordance with the guidelines outlined in this document. LA R.S. 46:2691 provides the State Treasurer with the authority to contract with outside money managers and the ability to pay the costs incurred for outside investment managers for the investment and management of the fund.

The State Treasurer shall establish rules and procedures for the investment of the Medicaid Trust Fund by outside investment managers (“managers”). The State Treasurer shall select outside investment managers through a competitive Request for Proposal (“RFP”) process.

## **III. INVESTMENT GOALS**

The Medicaid Trust Fund shall be prudently managed within the parameters established by the constitution and the laws of the State of Louisiana. The State Treasurer will seek three equally desirable long-term goals:

- A. To provide income in a stable and predictable fashion to the beneficiaries.
- B. Enhancement of market value of Medicaid Trust Fund through diversification
- C. Preservation of Medicaid Trust Fund’s capital

The State Treasurer shall have the authority and ability to review these goals from time to time for their continued feasibility and appropriateness, and to make revisions when necessary.

The State Treasurer shall strive to achieve a predictable level of income for the Medicaid Trust Fund beneficiaries. The interest income requirement of the Medicaid Trust Fund is substantial and continuous. The Medicaid Trust Fund needs to grow to ensure a perpetual benefit for the Fund beneficiaries. In addition, it is important to enhance the market value of the Fund and provide growth in real terms after the effects of inflation.

The State Treasurer shall attempt to meet these goals by maximizing the return on the Medicaid Trust Fund investments consistent with an appropriate level of risk and subject to a generation of adequate interest income. Additionally, the Medicaid Trust Fund shall be adequately diversified to provide reasonable assurance that an investment in any single asset class, security type, or industry group will not have an adverse impact on the fund.

## **IV. ASSET ALLOCATION**

Asset allocation can be a primary determinant of Medicaid Trust Fund investment performance, and is the responsibility of the State Treasurer. Asset allocation determines the appropriate weighing of bonds and other permitted investments that yield the best-expected return after adjusting for risk. The asset allocation may be changed from time to time based on the condition of the financial markets and the economy. Additionally, in establishing the investment goals and policies of the Fund, the State Treasurer shall consult no less frequently than semiannually with the secretary of the Department of Health and Hospitals as to the anticipated cash withdrawals from the fund during the next twelve months. In establishing the appropriate asset allocation, recognition of the role and relationship of various asset classes will be considered. These include:

### **Bonds**

The principal purpose of fixed income investments is to provide relative safety of principal and a predictable source of interest income.

### **Other Permitted Investments**

The principal purpose of other permitted investments is to provide relative safety of principal and additional sources of income.

### **Cash/Cash Equivalents**

The principal purpose of maintaining cash equivalents in the portfolio is to provide liquidity to meet the cash flow needs of the Medicaid Trust Fund beneficiaries. Cash and cash equivalents may also be used as a defensive strategy to protect the Medicaid Trust Fund from erosion of principal during unfavorable market conditions.

### **Target Asset Mix**

Currently, the Medicaid Trust Fund is not permitted to invest in equity securities and requires the passage of a constitutional amendment to do so. Therefore, the Fund's target asset mix will consist entirely of a broadly diversified portfolio of approved fixed income and short-term securities.

## **V. INVESTMENT GUIDELINES**

### **Fixed Income Investments**

The fixed income (bond) portion of the Medicaid Trust Fund portfolio shall be invested

in marketable fixed income securities. The following policies shall be strictly adhered to:

- A. Bonds purchased in any Medicaid Trust Fund portfolio should be selected for their expected annual income.
- B. Bonds purchased in any Medicaid Trust Fund portfolio should be selected for their expected return over a market cycle.
- C. Bonds should be selected with consideration for total return. Total return takes into consideration interest income and capital appreciation/loss.
- D. All fixed income (bond) investments shall be appropriately diversified by maturity, security, sector, and credit quality.
- E. Active management of the fixed income portfolio may be engaged. Active management permits shifting along the yield curve and sectors of the fixed income market.
- F. The Medicaid Trust Fund bond portfolio may not hold more than ten percent (10%) at cost of any issuer's securities other than direct obligations of the U.S. Treasury and/or U.S. Agencies.
- G. In order to benchmark and limit interest rate risk, the Medicaid Trust Fund bond portfolio shall have duration characteristics similar to the Lehman Brothers Government/Credit Bond Index (or similar fixed income index approved by the Treasurer of the State of Louisiana) and under no circumstances shall the Medicaid Trust Fund bond portfolio duration exceed 10.0 years.

**Acceptable Fixed Income Securities**

- A. The Medicaid Trust Fund may invest in direct general obligations or obligations, which are guaranteed by the United States Government.
- B. The Medicaid Trust Fund may invest in bonds, debentures, notes or other evidences of indebtedness issued by any of the following agencies of the United States Government: Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), Federal Home Loan Bank (FHLB), Student Loan Marketing Association (SLMA), Federal Farm Credit Bank (FFCB) and Small Business Administration (SBA).
- C. The Medicaid Trust Fund may invest in time certificates of deposits of state banks, national banks, savings and loan associations domiciled in the state of Louisiana. Investments in time certificates of deposits shall be conducted under the policy and guidelines of the General Fund of the State

of Louisiana.

- D. The Medicaid Trust Fund may invest in bonds, debentures, notes or other evidence of indebtedness issued by corporations or the United States. All corporate fixed income securities held in the Medicaid Trust Fund portfolio shall be rated investment grade credit quality classes of Moody's, Inc. (Baa or above) or Standard & Poor's Corporation (BBB or above).
- E. The Medicaid Trust Fund may invest in bonds, debentures, notes or other evidence of indebtedness issued by, and backed by the full faith and credit of, sovereign nations that are denominated in United States Dollars. All foreign fixed income securities held in the Medicaid Trust Fund portfolio shall be "A" or above by Moody's, Inc., "A" or above by Standard & Poor's Corporation, or the equivalent rating by a rating agency recognized by the National Association of Insurance Commissioners (currently Moody's, Standard & Poor's, Fitch's and Dominion Bond Rating Service).
- F. Should any security in a Medicaid Trust Fund portfolio be downgraded below investment grade by a rating agency, the investment manager must notify the State Treasurer of any such rating change along with the investment manager's plan for liquidating any such security.

#### **Fixed Income Investment Restrictions**

The State Treasurer and any investment managers for the Medicaid Trust Fund bond portfolio are restricted from the following activities:

- A. The purchase of bonds on margin.
- B. The short sale of any security.
- C. Unregistered private or direct placement of any kind.
- D. Debt securities of the custodian bank(s), investment advisor(s), broker dealer(s) or their parent subsidiaries entered into a contractual relationship with the State Treasurer or the Medicaid Trust Fund
- E. Direct loans or extension of lines of credit.
- F. Purchases of bonds denominated in foreign currencies, purchased on foreign exchanges, or cleared through foreign clearing entities.
- G. Direct purchases of single family or commercial mortgages.
- H. Any mortgage pass-through security such as, but not limited to, pass-through mortgage-backed securities (MBS), collateralized

investment  
zed debt obligations (CDOs) shall  
be subject to the constraints listed below.

1. U.S. Government and Government Sponsored Entity (GSE or Agency) guaranteed fixed and floating rate MBS, CMOs and REMICs can be held without limitation.
2. Private label CMOs, REMICs and CDOs are restricted to the following:
  - i. All collateral must be AAA rated
  - ii. Collateral commonly referred to as subprime or Alt-A are prohibited
  - iii. All collateral must be backed by first mortgage liens
  - iv. Sequential Pay (SEQ) tranches whose average life is less than 12 years
  - v. Planned Amortization Class (PACs) tranches that are Type I and whose average life is less than 12 years
  - vi. Scheduled Class (SCH) tranches whose average life is less than 12 years
  - vii. Accretion Directed (AD) tranches whose average life is less than 12 years
  - viii. Private label CMOs, REMICs and CDOs shall not exceed 35% of the portfolio
3. Inverse Floating Rate (Inverses), Interest Only (IOs), Principal Only (POs), Companion and Residual tranches of MBS, CMOs, REMICs and CDOs are prohibited regardless of issuer.
4. Targeted Amortization Class (TACs) and Accrual tranches of CMOs, REMICS and CDOs in aggregate will be limited to 5% of the mortgage securities portfolio regardless of issuer.
5. At the time of purchase any CMO, REMIC or CDO investment's price risk shall not exceed 25% change in market value at +/- 300bps stress test, and Weighted Average Life shall not to increase by more than 7 years at +300bps stress test.
6. In the event that other types of mortgage-related securities are developed that have risk characteristics similar to the permissible investments in this category the portfolio manager will first seek the approval of the Chief Investment

ring into any securities transactions involving any such security..

### **Cash/Cash Equivalent**

The principal purpose of maintaining cash equivalents in the portfolio is to provide liquidity for the cash flow needs of the Medicaid Trust Fund beneficiaries. Cash and cash equivalents may also be used as a defensive strategy to protect the Medicaid Trust Fund from erosion of principal during unfavorable market conditions.

Idle cash shall be invested daily. Idle cash shall be invested under the policy and guidelines of the General Fund of the State of Louisiana. 100% of the idle cash of the Medicaid Trust may be invested in any one of the following:

- A. Idle cash may be invested daily through an automatic sweep into the custodian bank short-term investment fund (STIF) or Money Market Mutual Fund (Money Market). To be eligible a STIF is restricted to those securities eligible for investment by the State Treasurer. To be eligible a Money Market must be organized as a Massachusetts Business Trust and invest solely in securities otherwise eligible for investment by the State Treasurer.
- B. Idle cash may be invested in commercial paper rated in the two highest credit quality classes of Moody's, Inc. (P1 or P2) or Standard & Poor's Corporation (A1 or A2).
- C. Idle cash may be invested in Repurchase Agreements.

## **VI. PERFORMANCE MEASUREMENT**

Medicaid Trust Fund investment performance will be measured by an unaffiliated organization with recognized expertise. To the extent possible, all performance measurement will be in compliance with the Association for Investment Management and Research (AIMR) performance presentation standards. Measurement will occur on a quarterly basis and will be used to evaluate the results of the total fund, asset classes, investment managers, and adherence to the guidelines.

### **Performance Goals**

Performance evaluations of the Medicaid Trust Fund will be conducted on an annual basis. Investment performance will be measured relative to the appropriate benchmark. Annual evaluations will examine the continued feasibility of achieving the Medicaid Trust Fund investment goals and objectives.

To accomplish the Medicaid Trust Fund investment objectives, it is critical to recognize the role of asset mix and specific performance goals that exist for separate asset classes. The achievement of these goals is most appropriately determined over a full market cycle. A full market cycle is generally a period of three to five years, or such period deemed to be appropriate by the Treasurer or the Treasurer's advisory committee or group.

Specific investment performance benchmarks for the Medicaid Trust Fund are:

### **Taxable Bonds**

An annualized total return equal to or greater than the Lehman Brothers Government/Credit Bond Index (or similar fixed income index approved by the Treasurer of the State of Louisiana) net of investment management fees, custodial fees, and transaction costs.

## **VII. INVESTMENT MANAGEMENT FIRMS**

### **Selection of Investment Mangers**

The State Treasurer shall follow a Request for Proposal process using a strict selection criteria based on sound investment industry principles for the selection of investment managers.

### **Investment Managers Must Meet the Following Criteria:**

- A. The investment manager must be a Registered Investment Advisor and in good standing with the Securities and Exchange Commission under the Investment Advisors Act of 1940, or in the case of a bank trust department, under the supervision and in good standing with the Office of the Comptroller of Currency and the Louisiana Office of Financial Institutions.
- B. The investment manager must provide five years of verifiable performance rates of return calculated on a time-weighted basis. These performance numbers must be based on a composite of fully discretionary accounts with a similar investment style and be reported net and gross of investment management fees.
- C. The investment manager must clearly articulate the investment philosophy and strategy that will be adhered to over time.
- D. Funds contracted with the investment manager for management purposes shall not exceed twenty percent (20%) of the firm's assets under

management in the style contracted.

- E. Investment managers shall be compensated on a basis point fee as a percentage of assets contracted to manage. Investment managers shall be paid in arrears on a quarterly basis.

**Duties and Responsibilities:**

- A. The investment manager shall manage the Medicaid Trust Fund assets under its care, custody or control in accordance with the objectives and guidelines set forth in this document, State Constitution, state laws, and rules promulgated by the State Treasurer.
- B. The investment manager shall have the discretion to invest a portion of Medicaid Trust Fund assets in cash reserves when deemed appropriate. The investment manager will be evaluated against peers for performance of funds under management.
- C. The investment manager shall promptly inform the State Treasurer in writing regarding any significant or material matters or changes pertaining to the investment of the Medicaid Trust Fund or in personnel within its organization. This would include, but is not limited to, the portfolio manager for the Fund, any principals of the firm and the director of research, if any.. Communication should be directed to the Treasurer, State of Louisiana, Post Office Box 44154, and Baton Rouge, Louisiana, 70804.
- D. The investment manager shall acknowledge and agree in writing to their fiduciary responsibility and to comply with the investment policy set forth in the contract and the investment objectives and guidelines for the Medicaid Trust Fund and as modified in the future.
- E. Investment managers shall appear before the State Treasurer at least once a year. Investment managers may be required to appear more frequently if deemed appropriate by the State Treasurer. During this appearance, the Investment Advisor must discuss the following:
  - 1. Review of portfolio goals and objectives.
  - 2. Review of the financial markets and economic outlook.
  - 3. Discussion of portfolio performance.
  - 4. Discussion of transactions, including brokerage.
  - 5. Material changes of staff and ownership of the firm.
- F. Investment managers shall submit quarterly a written performance report to the State Treasurer detailing investment performance. Quarterly reports shall be submitted in a timely fashion.

### **Investment Manager Review**

Investment managers are expected to perform in the top fifty percentile of their peer group. Should an investment manager fail to meet their performance benchmark within any rolling twelve (12) months, they will be placed under review.

Reviews will consist of the following:

- A. Scrutiny of the investment philosophy and process.
- B. Explanation of substandard performance to the satisfaction of the State Treasurer.
- C. Two additional quarters to bring investment performance up to standard without modifying the stated investment philosophy or strategy.

Failure to comply with the conditions resulting from being placed on review may result in termination of the investment manager's contract.

## **VIII. INVESTMENT CONSULTANT**

From time to time the State Treasurer may retain the services of an investment consultant for the purposes of assistance in the following:

- A. Establishing the appropriate asset allocation.
- B. Determination of appropriate equity manager styles (growth versus value, large capitalization versus small capitalization)
- C. Conducting investment manager searches.
- D. Determination of investment manager risk profile.
- E. Performance evaluation of investment managers.

### **Selection of Consultant**

The State Treasurer shall follow a Request for Proposal process using strict selection criteria based on sound industry principles for the selection of a consultant.

Investment Consultants Must Meet the Following Criteria:

- A. The investment consultant firm must have at least five years of experience consulting accounts with assets greater than \$250 million.

- B. The investment-consulting firm must have experience conducting investment manager searches and performance measurement for public funds with total assets greater than \$250 million.
- C. The investment consultant shall be paid in arrears quarterly basis.
- D. Any consultant that is a broker/dealer or investment manager, or that is affiliated with a broker/dealer or investment manager, must disclose the nature of the relationship. The investment consultant may not receive commissions or fees as a form of payment from any broker/dealer or investment manager that conducts business with the Louisiana State Treasurer.

## **IX. FUND ADMINISTRATION**

Administration is vital to the integrity of the Medicaid Trust Fund and necessary for the fulfillment of goals and objectives. The State Treasurer shall provide the appropriate internal controls and record keeping insuring the integrity of the Medicaid Trust Fund.

Transaction and accounting records shall be complete and prepared on a timely basis with consideration given to the adequacy of an audit trail. Custody of Medicaid Trust Fund assets shall be in compliance with applicable state laws and be arranged to provide as much security, trading speed, and fund accounting as possible. Adequate insurance levels will be maintained by the Medicaid Trust Fund custodian or agent contracted by the State Treasurer.

All securities transactions to purchase or sell shall be entered into on a “best execution” basis, yielding the best-realized net price. All securities transactions shall be conducted on a delivery versus payment basis.

On or before November first of each year, the State Treasurer shall prepare and submit a report on the performance of the Medicaid Trust Fund to the secretary of the Department of Health and Hospitals. The State Treasurer will also submit a copy of the report to the Joint Legislative Committee on Health and Welfare and the Senate Committee on Health and Welfare. Additionally, the State Treasurer shall report the status of the fund at least quarterly to the secretary of the Department of Health and Hospitals and the Intergovernmental Transfer Subcommittee.

## **X. INVESTOR RESPONSIBILITY**

As a shareholder, the Medicaid Trust Fund has the right to voice opinions in the corporate

affairs of companies owned by the fund. This includes the right and obligation to vote proxies in a manner consistent with the unique role and mission of the fund's beneficiaries, as well as, for the economic benefit of the fund. The Medicaid Trust Fund shall be the primary beneficiary of all investment decisions. The Medicaid Trust Fund shall not be invested to achieve temporary benefit for any purpose, including the use of its economic power, to advance any political or social cause.