



# DoD NAF Treasury Management Open Forum Meeting Minutes

November 14, 2018

## **Meeting Purpose & Objectives**

The DoD NAF Treasury Open Forum meeting is held annually, in accordance with enclosure 9 of Department of Defense Instruction (DoDI) 1015.15, "Establishment, Management, and Control of Nonappropriated Fund Instrumentalities and Financial Management of Supporting Resources," in order to provide a free exchange of information regarding treasury management practices.

The Marine Corps Community Services (MCCS) hosted the 2018 meeting.

## **Agenda Items**

- 1. Welcome and Overview**
- 2. Discussion of Current Economic and Investment Climate and Outlook**
- 3. NAF Inter-Service Borrowing (action item from last meeting)**
- 4. NAF Investment Performance Reporting: Realized Return versus Total Return (before and after expenses); Simple Return versus Dollar Weighted Return**
- 5. DoDI 1015.15 Update**
- 6. NAF Banking and Investment Rapid Improvement Event Recommendations (action item from last meeting)**
- 7. Closing Remarks**

## **Meeting Attendees**

- Mr. John Johnston, Marine Corps MCCS
- Ms. Pyper Brenner, Marine Corps MCCS
- Mr. Fred Stout, Marine Corps MCCS
- Mr. Laurent Lant, Army IMCOM G9
- Mr. Samuel Steffanina, Army IMCOM G9
- Ms. Nancy Stephens, Navy Commander, Navy Installation Command (CNIC)
- Ms. Tina Hudson, Air Force Services Agency, Financial Management (SVA/FM)
- Mr. AC Berry, Air Force SVA/FM
- Mr. Cameron Zablocky, Air Force SVA/FM
- Mr. Brian Poss, Army and Air Force Exchange Service (AAFES)
- Mr. William Moring, AAFES
- Mr. Tom McDonald, Navy Exchange Service Command (NEXCOM)
- Mr. Michael Curtis, OSD, Military Community and Family Policy

## Meeting Notes

### 1. Welcome and Overview – Ms. Pyper Brenner, Marine Corps MCCA (Meeting Host)

- a. Ms. Brenner welcomed the participants to the NAF Treasury Open Forum Meeting, hosted by the Marine Corps.

### 2. Discussion of Current Economic and Investment Climate and Outlook, Ms. Brenner, Marine Corps

- a. Ms. Brenner asked if anyone had any comments on the current economic and investment climate.
- b. Mr. Lant started with a statement that rising interest rates have started to worry investors. There have been three interest rate hikes this year by the Federal Reserve Bank (Fed), and there may be another one in December 2018. Mr. Lant anticipates further interest rate increases in 2019 and 2020. Consequently, the Army is changing its investment strategy to shorten its portfolio duration (i.e., average maturity of the portfolio) to no more than two years. The Army currently has a barbell strategy where its investment maturities are aggregated in the very short short-term (0-2 years) and longer-term (4-5 years), but not so much in the intermediate period (2-4 years). Mr. Lant said the change in the majority in the House of Representatives could have an impact on the market. Also, the London Interbank Offered Rate (LIBOR) is being replaced by the Secured Overnight Financing Rate (SOFR) in 2021 and this could be a factor to the investment climate.
- c. Mr. Stout agreed with Mr. Lant's statements and added that oil prices are on the rise. For the Marine Corps, about 45 percent of its portfolio matures in 2019. Investing in shorter term maturities in 2018 utilized the steepest portion of the allowable yield curve. This strategy should allow the investment fund to generate a projected \$3.5 million in additional revenue in 2018.
- d. Mr. Moring said that AAFES, as the biggest borrower among the DoD NAFIs, focuses their purchases on overnight investments. AAFES is contemplating going out as far as 60 days or longer on some of its portfolio, but not as far out as 270 days. Mr. McDonald asked about the rate range from overnight investments compared to those for 270 days. Mr. Moring said the overnight rate currently is 0.219 (219 basis points) and the 270 day rate currently is 0.272.

- e. Mr. McDonald said that NEXCOM is also keeping its portfolio duration less than two years. Mr. McDonald asked if anyone was investing in Treasury Inflation-Protected Securities, or TIPS. Mr. Steffanina said that Army was looking at them, but had not yet purchased any. Mr. Lant said that Army was looking at investments with floating interest rates, such as mortgage-backed securities and callable bonds.

### **3. Inter-Service Borrowing – Mr. Michael Curtis, MC&FP**

- a. Currently, DoDI 1015.15 (paragraph 6.10) prohibits loans between DoD Components. One of the action items from the 2017 Open Forum meeting was for CNIC to draft a unified legislative and budgeting (ULB) package to seek a change to this policy. A ULB was thought necessary, since the prohibition on inter-Service borrowing came from directive language in a House of Representatives conference report (103-701), as part of the Fiscal Year 1995 National Defense Authorization Act. CNIC also volunteered to prepare an analysis that showed that increased NAF interest income and decreased NAF interest expense derived from inter-Component borrowing, compared to utilizing commercial loans, could help provide justification for the policy change.
- b. During the year, Mr. Curtis worked with MC&FP's congressional/legislative affairs staff and MC&FP's point of contact at the Office of the Assistant Secretary of Defense for Legislative Affairs to ask Congress if they would allow OSD to change the policy. After many months of questioning congressional staffers on the issue, the message to MC&FP was there was no issue with OSD changing the policy. Consequently, there is no need for the ULB.
- c. Mr. Curtis said that the change would be made in the update of DoDI 1015.15. Mr. McDonald asked if there was a faster way to make the change in policy. Mr. Curtis said that a directive-type memo (DTM) could be published faster than the DoDI 1015.15 and said that he will look into a DTM as an option.

### **4. NAF Investment Performance Reporting: Realized Return versus Total Return (before or after expenses) – Mr. Laurent Lant, Army IMCOM G9**

- a. Mr. Lant started the discussion with the question of the best way to measure performance for the NAFI investment portfolios. Currently, DoDI 1015.15 requires the NAFIs to report both total rate of return and realized return on their investments.
- b. Total rate of return includes unrealized gains and losses and can be misleading because Army has an investment strategy to hold their investments to maturity. It is very rare to sell investments before their

maturity date. The inclusion of unrealized gains and losses in the total return calculation can cause the total return to be very different from the realized return. The realized return reflects the most likely rate of return, since the NAFIs hold their investments to maturity. Mr. Lant suggested that the NAFIs stop reporting total rate of return and only report realized return.

- c. Mr. McDonald agreed with Mr. Lant and asked the group if there were any NAFIs that do not hold their investments to maturity. Mr. Berry said the Air Force has a buy and hold strategy. There was consensus that all DoD NAFIs have an investment strategy to hold their investments to maturity.
- d. Mr. Curtis asked if there was any advantage to report the total rate of return. If everyone is holding their investments to maturity, then is it not confusing to a lay person to include total rate of return? Mr. Lant said yes. He said another disadvantage of reporting total rate of return is the investment balances can show as negative, if there are significant unrealized losses. Such losses are unlikely to be realized since the investment will be held to maturity with a positive return.
- e. Mr. Stout said that when DoDI 1015.15 was last revised, there was a focus on the yield earned by the NAFIs and total rate of return was added to the annual report so that the NAFIs could be compared to benchmarks (investment yields of similar investment portfolios outside of DoD). Mr. Stout said that the focus of the annual reporting should be on safety and liquidity, with less emphasis on yield.
- f. Mr. Lant said that reporting the expenses incurred by each of the NAFI investment operations is problematic because each NAFI records their expenses differently. Mr. Stout agreed. He said that comparing the investment-related expenses for each of the NAFIs is like comparing apples to oranges.
- g. Mr. Curtis said he understands the issues, but there needs to be a good reason to change the policy. What are the pros and cons to making the changes?
- h. Mr. Lant said the use of the benchmarks must also be reviewed. Mr. McDonald agreed. The benchmarks are difficult to choose because they often do not have the same durations as the DoD NAFI portfolios. Often, the benchmarks do not match the reality of the NAFI portfolios.
- i. Mr. Curtis said he will put together a summary of the current proposed changes to the investment section of DoDI 1015.15, including the change to policy on inter-Service borrowing, and send the draft out to the group for preliminary review. That document can be used as a starting point to the other changes discussed today.

## 5. DoDI 1015.15 Update – Mr. Curtis, MC&FP

- a. Mr. Curtis asked if there were any other suggestions for changing DoDI 1015.15. There were none from the group.

## 6. NAF Banking and Investment RIE Recommendations – Mr. Curtis, OSD, MC&FP

- a. The second of two action items from the November 2017 Open Forum meeting was for Mr. Curtis to send to each of the Service NAF Treasury Managers the 49 recommendations that were developed during the 2013 rapid improvement event (RIE) to see if any were still relevant. Two of the 49 were deemed relevant at the 2017 meeting and should remain as active recommendations: 1) incorporating piggyback clauses into contracts, and 2) the update of the DoDI 1015.15.
- b. The feedback received from the group was that there were no additional RIE recommendations that were still relevant.

## 7. Closing Remarks

- a. Ms. Brenner asked if there were any other topics for discussion. Mr. Steffanina mentioned that the current Administration was looking into privatizing some government agencies, such as the Federal Home Loan Mortgage Corporation (Freddie Mac) and the Federal National Mortgage Association (Fannie Mae). Such actions could impact the list of issuers where the DoD NAFIs can invest.
- b. Ms. Brenner thanked everyone for attending the meeting and contributing to the effort to share ideas with the group.

## Action Items:

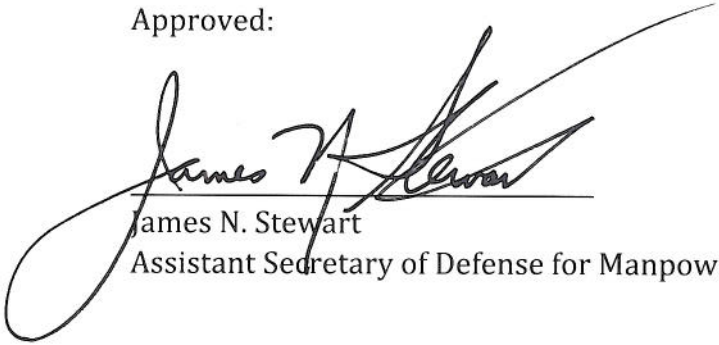
Item	POC
MC&FP will make the change to DoDI 1015.15 to allow inter-Service borrowing.	Mr. Michael Curtis
MC&FP will explore the possibility of making the change to policy regarding inter-Service borrowing in a directive-type memorandum.	Mr. Michael Curtis
MC&FP will consider changing the annual NAF Treasury and Investment reporting regarding such topics measuring the performance of the investment funds, benchmarks, and investment operations expenses.	Mr. Michael Curtis

MC&FP will summarize the proposed changes to the investment section of DoDI 1015.15 to the NAF investment managers for preliminary comments.

Mr. Michael Curtis

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Approved:



James N. Stewart  
Assistant Secretary of Defense for Manpower and Reserve Affairs