



DoD Nonappropriated Fund Treasury Oversight Committee Meeting Minutes

April 27, 2018

Meeting Purpose & Objectives

The DoD Nonappropriated fund (NAF) Treasury Oversight Committee meets annually in accordance with DoD Instruction (DoDI) 1015.15, "Establishment, Management, and Control of Nonappropriated Fund Instrumentalities and Financial Management of Supporting Resources."

Agenda Items

- 1. Welcome and Overview**
- 2. Discussion of Current Economic and Investment Climate and Challenges**
- 3. Discussion on Steady Increase of Current NAF Investment Balances in Declining Appropriated Fund (APF) Budget Environment**
- 4. Data Repository and Tableau – Realized Return versus Total Return on Investment**
- 5. Results of DoDI 1015.15 Policy Compliance Review**
- 6. 2017 NAF Treasury Open Forum Meeting**
- 7. Status of Revision of DoDI 1015.15**
- 8. Portfolio Review/Annual Cash and Investment Management Reports**
 - a. Air Force MWR**
 - b. Navy Commander, Navy Installations Command (CNIC)/N9**
 - c. Marine Corps Community Services (MCCS)**
 - d. Navy Exchange Service Command (NEXCOM)**
 - e. Army Installation Management Command (IMCOM) G9**
 - f. Army and Air Force Exchange Service (AAFES)**
- 9. Open Discussion**
- 10. Wrap-Up**

Meeting Attendees

- Mr. Justin Hall, OSD, MC&FP – Committee Chair
- Ms. Paulette Freese, OSD, MC&FP
- Mr. Michael Curtis, OSD, MC&FP
- Ms. Coleen Amstein, Army M&RA
- Mr. Eric Alberts, Army M&RA
- Mr. Gerald Holliday, Army FM&C
- Mr. Paul Burk, Army IMCOM G9
- Mr. Josh Gwinn, Army IMCOM G9
- Mr. Laurent Lant, Army IMCOM G9
- Mr. Sam Steffanina, IMCOM G9
- Mr. Robert Ramsey, IMCOM G9
- Mr. Matthew Keathley, Navy CNIC
- Ms. Annie Fowler, Navy N46
- Ms. Katy Bloomberg, Navy N46
- Ms. Evonne Carawan, OASN(M&RA)
- Mr. John Johnston, Marine Corps MCCA
- Ms. Pyper Brenner, Marine Corps MCCA
- Mr. Fred Stout, Marine Corps MCCA
- Lt Col Chip Hollinger, SAF-MRR
- Col Jennifer Nevius, AS/A1
- Mr. Mark Montgomery, AF/A1
- Ms. Tina Hudson, Air Force SVA/FM
- Mr. Scott Howard, Air Force SVA/FM
- Mr. AC Berry, Air Force SVA/FM
- Mr. Cameron Zablocky, Air Force SVA/FM
- Mr. Wally Erck, Air Force SAF/FMCEB
- Ms. Teresa Asbury, Air Force SAF/FMCEB
- Ms. Laura Beal, Air Force SAF/FMCEB
- Mr. Brian Poss, AAFES
- Mr. William Moring, AAFES
- Mr. Andrew Howell, NEXCOM
- Mr. Tom McDonald, NEXCOM

Meeting Notes

1. Welcome and Overview – Mr. Justin Hall, OSD

Mr. Hall opened the Committee meeting by thanking the Military Services and Military Service exchanges for their attendance and participation. He acknowledged the importance of managing such large portfolios well and further noted that such a task was inherently challenging.

2. Discussion of Current Economic and Investment Climate and Challenges – Mr. Michael Curtis, OSD

- a. Mr. Mike Curtis began the discussion by asking the attendees about their thoughts on the current economic and investment climate and what challenges they anticipated going forward. Mr. Curtis commented that the early indicators from the Federal Reserve (the Fed) suggested that two interest rate hikes were likely to take place in 2018.
- b. Mr. Matthew Keathley speculated that the Fed may raise interest rates. He added that inflation may rise to between 3% and 4%, which might cause the Fed to raise interest rates. Overall, Mr. Keathley did not believe these actions would hurt the economy in any significant way, as the economy was going strong.
- c. Mr. Fred Stout commented that the money supply was so tight that increasing rates too quickly may create an inverse yield curve and trigger a recession. Mr. Stout further noted that indicators showed that the Fed board members may support three rate hikes.
- d. Mr. William Moring noted that the market tended to be short-sighted, and moderate increases in volatility would not have significant impact on the NAF investment portfolios, especially since a large portion of the portfolios was held to maturity anyway.
- e. Mr. Laurent Lant commented that the government appeared to be shifting away from monetary policy to fiscal policy as the means of managing the economy. With this strategic shift, there is concern that the Fed may start selling bonds to decrease the federal portfolio in that area. Mr. Lant noted that while spending has increased in light of the tax cut policy, there was reason for caution given the lack of an increase in long-term interest rates. Mr. Lant anticipated the short-term rate to be increased in June and September, did not view inflation as a concern, and also didn't anticipate the interest rate hikes having success in reducing volatility. He added that volatility could have a severe impact on the total return on the NAF portfolios.
- f. Mr. Keathley anticipated that the current situation of being close to an inverted yield curve would correct itself soon, as the 30-year yield curve for Treasury notes would raise significantly higher than the 10-year curve. Mr. Keathley

currently noted that the 17 to 18 basis point difference between the 30-year rate and the 10-year rate was a rare situation and showed the need for inflation.

3. Discussion of the Steady Increase of Current NAF Investment Balances in Declining APF Budget Environment – Mr. Michael Curtis, OSD

- a. In order to reduce the perceived high NAF cash balance at CNIC, the Navy Financial Management Budget (FMB) shop within the Assistant Secretary of the Navy, Financial Management and Comptroller, chose to reduce APF funds to CNIC, in order to “spend down” NAF cash FY 2014 and FY 2015. Unfortunately, the actions have had unintended consequences with Navy currently having a very low cash balance. Programmed APF funds have not increased, impacting FY 2016 through FY2018 cash balances.
- b. Mr. Hall stated that the APF policy funding standard for Category A and B MWR programs is to fund all costs authorized APFs with APFs. It appeared some Services were viewing the 85% and 65% funding standards for Category A and B MWR programs as ceilings rather than floors as intended, and were not providing necessary APF funds to flow to Category A and B MWR programs.
- c. There was a general discussion of funding for MWR programs and the challenges to meet or exceed the 85% and 65% funding standard metrics. Mr. Hall said that he appreciated the scope of the problem and was happy for the discussion, but fixing the problem was beyond the scope of the NAF Treasury Oversight Committee. The MWR and Resale Policy office in conjunction with the Military Departments is leading a review of the policies for APF support of MWR programs.

4. Data Repository and Tableau – Realized Return versus Total Return on Investment – Mr. Michael Curtis, OSD

- a. Mr. Curtis then turned to the Tableau visualization read-ahead that showed the total return vs realized return for each of the NAF portfolios. Mr. Curtis noted that total return had reporting inconsistencies, with some Services using a monthly average in their reports, while others reporting a sum or input using an independently calculated figure.
- b. Mr. Stout commented that total return takes change in price into consideration, not just change in interest income. Mr. Johnston said that total return takes into consideration unrealized gains and losses. Considering that the Marine Corps and other Services and exchanges generally hold their investments to maturity, the total return metric was not as relevant to investment performance as the realized return. Mr. Curtis noted that current policy requires both metrics, but perhaps consideration should be made to de-linking the two in the annual report. Mr. Tom McDonald stated that NEXCOM has never sold any treasuries, always holding

them to maturity. Mr. McDonald added that there was no value in keeping total return in his opinion.

- c. Mr. Stout pointed out that the purpose of these investment funds was not comparable to the goals of a mutual fund. The primary goal was meeting cash flow demand, and thus maintaining a large portfolio of investments with high liquidity. Return on this pool of capital was not the major goal.
- d. Mr. McDonald commented that the issue of comparability between the portfolios was distorted by the duration of the portfolio. Each Service in meeting its own cash flow needs, may manage investments to emphasize short or long-term investing. This choice greatly impacted the return metrics.
- e. Mr. Keathley agreed that duration had significant effect on metric comparability, but noted that the metrics could still be useful to DoD leadership in highlighting outliers such as a high negative value or a significant departure from portfolio return vs similar investment return.
- f. Mr. Curtis agreed with the basic premise that safety and liquidity were the top DoD policy goals for these investment portfolios, but added that yield data was good to have.
- g. Mr. Hall added that the funds were difficult to compare to one another and draw meaningful conclusions at current state. Exchange service requirements for inventory turnover drove a shorter duration (i.e., 6 months) while the MWR funds were able to handle a longer investment duration (i.e., 1 year). He agreed that duration requirements for each type of organization needed to be emphasized in the annual treasury reports in some way.
- h. Mr. Lant noted that even the Realized return metric had issues. Mr. Lant contended that the DoD policy did not give a clear definition of accrued interest. Mr. Lant further stated that the use of weighted dollars in the return metrics caused distortions. He recommended usage of simple return as opposed to realized return and removal of weighted dollars.
- i. Mr. Curtis recommended one-on-one meetings between OSD and the NAF portfolio managers to discuss and hopefully gain consensus on the nature of the disclosures and what should be added or adjusted in the DoDI 1015.15.

5. Results of DoDI 1015.15 Policy Compliance Review – Mr. Michael Curtis, OSD

Mr. Curtis then turned to the DoDI 1015.15 compliance review. Mr. Curtis noted that the DoDI 1015.15 was under review and that input from previous Treasury meetings had been incorporated into the draft policy document. Mr. Curtis noted that everyone passed the policy compliance review for calendar year 2017.

6. 2017 NAF Treasury Open Forum Meeting – Mr. Michael Curtis, OSD

Mr. Curtis noted that the minutes from the NAF Treasury Open Forum meeting in November 2017 were still in draft and being reviewed. Every attempt would be made to get them signed and sent out to the Committee as soon as possible. On the subject of the desire to change the policy to allow inter-Service borrowing, Mr. Curtis said that he was working with the Congressional/Legislative Affairs team in MC&FP to have the Office of the Assistant Secretary of Defense Legislative Affairs team discuss the issue with the Congressional staffers. The hope is that Congress will have no issue with changing the policy.

7. Status of Revision to DODI 1015.15 – Mr. Michael Curtis, OSD

- a. Ms. Carawan stated that the Department of Navy stakeholders would like to see DoDI 1015.15 reissued soon. She asked if there is anything the Services could do to help OSD.
- b. Mr. Hall noted that there were program and financial review pieces in the DoDI 1015.15 that required OSD action and agreed that the policy needed to be reissued soon. He added that issuance of up-to-date policy documents were a high priority for the MWR and Resale Policy office.

8. Portfolio Review/Annual Cash and Investment Management Reports

- a. Air Force. As of December 31, 2017, the Air Force had an investment balance of \$1.5 billion and a realized return of 1.26%. The portfolio's average days to maturity (i.e., duration) was 856 days. The Air Force also had a \$38 million letter of credit with J.P. Morgan Chase. Their audit was ongoing and will be submitted once completed.
- b. Navy/CNIC. Navy's investment balances at December 31, 2017, was \$799 million. Their realized return was 1.54%. The portfolio's average days to maturity was 541 days. CNIC continued to value a line of credit agreement with NEXCOM that was mutually beneficial, providing lower interest costs for NEXCOM and higher interest income for CNIC than available with any arrangement on the market. CNIC's audit was ongoing and will be submitted once completed.
- c. Marine Corps/MCCS. The investment balance for MCCS at December 31, 2017, was \$529 million with a realized return of 1.13%. The portfolio's average days to maturity was 437 days. Mr. Stout mentioned the Marine Corps began implementing a shared services center in Kansas City, MO a year ago to support payroll, finance, and accounting transaction processing across Headquarters Marine Corps and all installations. Initial operating capability was reached last year, and they continue to migrate installation activity. The transition was expected to be completed in 2019. Their financial statement audit was in progress and will be submitted once completed.

- d. NEXCOM. The investment balance for NEXCOM at December 31, 2017, was \$289 million, with a realized return of 0.91%. NEXCOM portfolio's average days to maturity was 181 days. The investment balance for Military Sealift Command was \$597 thousand with a total return of 0.81%. Their audits were in progress and will be submitted once completed.
- e. Army/IMCOM G9. Army's investment balance was \$1.61 billion at December 31, 2017, with a weighted total return of 1.27%. The portfolio's average days to maturity was 430 days. Their audit of the Army Banking and Investment Fund was in progress and will be submitted once completed.
- f. AAFES. As a net borrower, the investment balance for AAFES was only \$34.7 million at December 31, 2017, with a total return of 0.81%. The portfolio's average days to maturity was 188 days. Their audit was in progress and will be submitted once completed.

9. Open Discussion

- a. No additional items were discussed.

10. Wrap-up – Mr. Michael Curtis, OSD

- a. Mr. Hall thanked the Services for submitting and presenting their reports and for their interest in increasing Inter-Service/Exchange cooperation.
- b. Summary of actions and due outs:
 - All Components to provide audit reports when they are complete.
 - MWR and Resale Policy office will incorporate average days to maturity/duration into future review and analysis of annual reports when comparing the NAF portfolios.
 - MWR and Resale Policy office will continue to pursue Congress' interest in a change to the policy to allow inter-Service borrowing.
 - MWR and Resale Policy office to schedule one-on-one meetings with the Services and exchanges to discuss changes to the policy and/or disclosures on the subject of realized return and total return.

Next Meeting: May 2019


Justin W. Hall, Committee Chairman

Date: 8/14/18

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Approved:

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