



Minutes of the Cash Management Policy Board  
Buena Vista Conference Center – 02/27/15

**Attendance:**

Member	Present
J. Flynn Jr, Chair	Yes
M. Morton	Yes
M. Karia	Yes
D. Marvin	Yes
T. Cook	Yes
J. Bullock	No
W. Engle	Yes
K. Simpler	Yes

**Others Present:** E. Black, S. McVay, C. Kurtzman, J. Johnstone, J. Hoover, R. Jaffè, W. Lane, L. Gerard

**1. Call to Order**

Mr. Flynn calls the meeting to order.

**2. Approval of November 5, 2014 Minutes**

Mr. Flynn asks for comments on the minutes.

Mr. Stephen McVay, Director of Finance and Treasury Services, notes that Margaret Iorii is no longer a member of the Cash Management and Policy Board and should be removed from the minutes.

The minutes are accepted without objection. Mr. Engle and Mr. Simpler abstained from voting as they did not attend the prior meeting.

**3. Review of 2014 CMPB Annual Report**

Mr. Simpler defers to Mr. McVay on reviews of the annual report. Mr. Simpler asks the members for feedback on whether the annual report provides valuable content or whether the report could use format and substance revisions.

Mr. Flynn asks if the 2014 report is calendar or fiscal year.

Mr. McVay confirms the report is fiscal year.

Mr. Flynn asks if the report has been submitted

Mr. McVay states that submission is awaiting approval.

Mr. Flynn asks if the report has been received by the Cash Management and Policy Board.

Mr. McVay confirms the report has been distributed.

Mr. Flynn requests any commentary.

Mr. Engle asks if the report could be made available sooner since we are currently more than six months past the end of the fiscal year.

Mr. McVay states that this year's report was delayed by the transition at the Office of the State Treasurer. Mr. McVay states that the annual report is typically completed by early October.

Mr. Engle moves the report is approved for distribution. Mr. Karia seconds. The motion carries without opposition.

Mr. Flynn request the report is forwarded to the Governor and the legislature.

Mr. McVay states the report was previously sent to the Governor and the Joint Finance Committee.

Mr. Morton states that he will ensure all the legislators receive the report if it is forwarded to him. Mr. Morton notes that the Office of the State Treasurer can handle distribution to the Governor.

#### **4. Banking Committee Report**

##### **a. EPX contract extension discussion**

Mr. Flynn asks about which point on the agenda Mr. Simpler intends to move for an executive session.

Mr. Simpler states that the executive session may be valuable for the investment advisor discussion.

Mr. Flynn asks for a discussion of upcoming banking contracts during the Banking Committee report to simplify organizational requirements as a result of the executive session.

Mr. Simpler agrees but asks that the Cash Management and Policy Board refer to the full schedule of contracts being discussed once the investment advisor discussion is broached.

Mr. Engle requests that the delegates from the Office of the State Treasurer report on the background due diligence regarding EPX and their associate business Bank Corp.

Mr. Simpler states that EPX is a technology company handling merchant services' data flow. EPX transmits this data to a sponsoring bank. Mr. Simpler states that their sponsoring bank at present is Bank Corp and that Bank Corp facilitates the movement of money through electronic transitions. Mr. Simpler states that EPX used their bankruptcy to sell their assets—their technology—to the company "NAB". NAB is a holding company for other merchant services companies. Mr. Simpler states that NAB appears to be spreading EPX's technology over their affiliates while keeping EPX as another separate subsidiary.

Mr. Simpler states that sponsoring banks and others pushed EPX towards new ownership in order to increase efficiency and the creditors of the old EPX have been fully satisfied in the bankruptcy proceedings. Mr. Simpler states that the Office of the State Treasurer is satisfied that the subsidiary that is now EPX is financially stable and that Delaware has experienced no technological disruption. Mr. Simpler notes that EPX has allowed for a short extension notification period to enable discussion at today's meeting and ensured that a project EPX is working on currently will not lead to developmental fees for the state in the next twelve months.

Mr. Engle notes that that the Cash Management and Policy Board's concern was an operational risk. Mr. Engle notes EPX went through bankruptcy without any operational glitches and that fallback protocols exist in the event of technological failure.

Mr. McVay states that both NAB and Bank Corp are backstops for EPX and would be able to keep that operation running for a minimum of twelve months. Mr. McVay notes that the card industry is heavily involved in protecting the smooth provision of these services.

Mr. Simpler states that Bank Corp, which only has a contractual relationship with EPX, has had a rough couple of quarters. Mr. Simpler notes that the credit risk associated with Bank Corp is not massive since Delaware's transactions are only on Bank Corp's balance sheet for roughly a day at a time. Mr. Simpler estimates the value of this credit risk to be between one or two million dollars at its highest and that Delaware could fairly seamlessly step away from Bank Corp should EPX become concerned with Bank Corp's sponsorship. Mr. Simpler notes again that the card associations have an interest in ensuring that systemic weak-links are seamlessly replaced. Mr. Simpler states that Bank Corp's operations should continue to be monitored, but that their core operations appear to be sound.

Mr. Engle states that Bank Corp is a well-capitalized bank and FDIC insured. Mr. Engle asks for a one year extension of EPX's contract since the time and effort required to issue a Request For Proposals (RFP) and exit the current arrangement would be considerable. Mr. Engle notes that the people using EPX's systems are happy with the product and state that the process is pain free.

Mr. McVay states that there has not been any negative feedback regarding EPX.

Mr. Engle moves that EPX's contract is extended until May of 2016. Mr. Simpler seconds the motion.

Mr. Flynn asks if this is the final year of EPX's contract.

Mr. Simpler states that there is one more extension after this one.

Mr. McVay states that once all extensions are applied there would be no need for further RFPs until May 2017.

Mr. Engle states that the situation will continue to be monitored closely. The motion carries unopposed.

**b. Banking Contract Considerations**

Mr. Simpler notes that the discussion to follow will be a full long term road map of future contractual considerations and that the Office of the State Treasurer intends to come to the Cash Management and Policy Board with requests a full twelve months prior to any RFPs if that is acceptable.

Mr. McVay states the contract extensions to be considered all expire December of 2015. This includes contracts with PNC Bank for disbursement of Delaware's checks and ACH payments, maintenance of the unemployment insurance lockbox and the training tax lockbox. Mr. McVay states that these three contracts are separate, but concurrent and that the operational process with PNC has been nearly flawless. Mr. McVay notes that the extensions would run until December 31<sup>st</sup>, 2016 and an RFP will be required for these processes in 2016.

Mr. McVay states that the Wells Fargo direct deposit contract is up for a one year extension to December 31<sup>st</sup>, 2016 and that an RFP for this contract would be required in 2016. Mr. McVay notes that the payroll and human resource agencies are content and have no issues with this contract.

Mr. McVay states that a lockbox processing contract for Corporate Franchise Fees with JP Morgan Chase is up for a one year extension to December 31<sup>st</sup>, 2016. Mr. McVay notes that the person with direct oversight of this program would like an extension.

Mr. Engle motions for the extension of these five contracts. Mr. Marvin seconds the motion. The motion carries unopposed.

Mr. Flynn asks if there is one contract out for proposal currently.

Mr. McVay states that there is an RFP in process for the electronic collection contract which is currently held by Bank of New York Mellon. Mr. McVay states that the RFP has received seven responses. Mr. McVay notes that electronic collections is the hub for electronic receipts from a variety of agencies and is also how money is sent out to satisfy the PNC disbursement accounts and any other obligations. Mr. McVay states that two to three finalists including the incumbent will be considered and that the current contract expires in August of 2015.

Mr. McVay advises the Cash Management and Policy Board on the upcoming RFPs for 2016. Mr. McVay states that the Wells Fargo direct deposit contract will be out of extensions and require an RFP. Mr. McVay states that the prepaid card agreement with JP Morgan Chase expires in June 2016 and has no extensions available. Mr. McVay states that JP Morgan is getting out of the prepaid card business and that an RFP will be necessary.

## **5. Update of Guidelines for Land and Water**

Mr. Flynn asks about the timing of guideline approvals for the reserve and liquidity accounts as well as the land and water account.

Mr. Edward Black, Deputy Attorney General, states that the general guidelines have gone through without a hitch. Mr. Black states that the land and water trust fund regulations were promulgated December 1<sup>st</sup> and their comment period has passed without comment. Mr. Black states that the land and water regulations are effective though the final publication has not come out yet. Mr. Black thanks Jeff Hoover, Stephen McVay, and Mike Karia for their oversight in the regulatory process. Mr. Black states that his position is historically contained in departments and agencies and that his assignment pertained to particular issues which are now resolved. Mr. Black states that he does not believe he will be involved with the Cash Management and Policy Board in the future.

Mr. Flynn asks who will handle the editing of the general guidelines.

Mr. Black states that he will be making the edits.

Mr. Flynn states an appreciation for what Mr. Black has done for the Cash Management and Policy Board.

Mr. Engle seconds Mr. Flynn's sentiment.

## **6. Investment Committee Report**

Mr. Simpler states that the majority of time recently has been focused upon the land and water RFP. Mr. Simpler states that the Office of the State Treasurer did not vary from the guidelines given, but that the RFP had gone out before reaching the Investment Subcommittee.

Mr. Hoover states that the RFP went out on the 16<sup>th</sup> of February.

Mr. Flynn asks about the process for the RFP. Mr. Flynn notes that questions from potential investment managers should be in by next week and that proposals should be in by the end of March. Mr. Flynn asks if recommendations could be possible by the June meeting of the Cash Management and Policy Board.

Mr. Simpler states that there is reason to have an additional Investment Subcommittee and Banking Subcommittee meeting before the June Cash Management Policy Board meeting. Mr. Simpler states that an assessment of the proposals received and some idea of the recommended managers should be developed by the Office of the State Treasurer before said Investment Subcommittee meeting.

Mr. Hoover states that there have been three to four specific enquiries, but no other good indication of how many managers will respond to this RFP. Mr. Hoover invites members to join the RFP committee.

Mr. Marvin notes that selection will be three managers and asks if the RFP process will involve interviewing six to eight managers.

Mr. Hoover states that fifty to sixty may reply, but that the interview process will be more like a top ten.

Mr. Marvin notes that it will likely be most convenient to do the interviews in Dover and suggests that Mr. Karia be involved in the RFP process as he lives near Dover. Mr. Marvin notes that Mr. Karia did well the last time managers were selected and has shown good judgment in the past.

Mr. McVay notes that Mr. Karia was very helpful as a member of the prior manager selection process and that the rest of the panel included several member of the Office of the State Treasurer and advising from Credit Suisse. Mr. McVay states that part of the RFP involves the proposing vendors' provision of historical data in a spreadsheet developed by Credit Suisse.

Bill Lane, Vice President at Credit Suisse, states that scoring and steps for the land and water RFP are the same as those used for the general investment manager RFP.

Mr. Marvin notes that the guidelines are broad enough so that the Delaware Community Foundation can be considered a candidate; regardless of whether they end up being selected.

Mr. Karia states he would be glad to work on the selection committee and honored as well.

Mr. Flynn asks if another member will be participating.

Mr. Simpler states that he will be involved as well.

Mr. Marvin states that he is available to provide oversight and consultation.

Mr. Flynn turns discussion to the overview of investment contract extensions and potential proposals.

Mr. Simpler notes that the advisor contract with Credit Suisse expires in May, but that the advisor contract will have to be discussed later in the meeting after Credit Suisse presents concerning the portfolio's performance.

Mr. McVay states the only extension is for the custodian contract with Bank of New York Mellon which expires December 2015 and warrants a one year extension. Mr. McVay states that Bank of New York Mellon is of the highest quality, responsive, and easy to work with. Mr. McVay notes that Bank of New York Mellon has had this custodian contract, subject to standard review and renewal, for at least the past ten years.

Mr. McVay notes that the investment manager contracts will end in May of 2016 and the recommendation here is to go to RFP for the reserve manager space.

Mr. Simpler suggests postponing the discussion of the reserve manager RFP until after Credit Suisse's presentation. Mr. Simpler notes that nine manager contracts expire in May 2016 and that each contract has two one year extensions. Mr. Simpler notes that the advisor contract, the custodian contract, and all the investment manager contracts being up for extension, bid, or renewal leaves the entire architecture of Delaware's investment structure variable in the next two and a half years.

Mr. Marvin states that he is disappointed with the custodian as he feels they let Delaware down in 2008/09 and that they were not bringing any judgment to bear on the positions taken in the investment portfolio. Mr. Marvin states he will go along with keeping them but that he shouldn't make the motion.

Mr. Flynn asks when the custodian contract runs out.

Mr. McVay states that the contract ends December of 2015.

Mr. Flynn suggests that Mr. Marvin and staff reach out to Bank of New York Mellon in order to discuss Mr. Marvin's concerns. Mr. Marvin notes that it is possible that the custodian is doing exactly what we are paying them to do and that he is merely misinterpreting their required role.

Mr. Flynn suggests reporting back at the meeting in June.

Mr. McVay states that if we were doing an RFP for this contract, it should have already been published in terms of time required to review the proposals. Mr. McVay states that the custodian transfer process may be time consuming.

Mr. Marvin states that he has no problem with an extension, but that he would like to have a conversation clarifying the custodian's responsibilities.

Mr. McVay notes that the security lending program, which performed poorly, is now gone. Mr. McVay states that all the custodian does now is provide safeguarding and accounting for investments plus audited financial statements and various financial reporting. Mr. McVay states that other requirements the Cash Management and Policy Board might consider, such as security lending, might be better overseen by the advisor or investment managers.

Mr. Marvin notes that the custodian was deafeningly silent on the losses brewing in the security lending segment and that the Cash Management and Policy Board did well to take small losses and run despite the lack of input.

Mr. Karia motions to extend the custodian contract. Mr. Morton seconds.

Mr. Engle states his support and concurs with Mr. Marvin on the need to make certain that the custodian has expectations congruent with those of the Cash Management and Policy Board.

The motion passes unopposed.

## **7. Review of Investment Results**

Mr. Lane introduces the other representatives from Credit Suisse.

Mr. Richard Jaffè, Managing Director at Credit Suisse, states that Credit Suisse is focused on listening and being available to as many people as possible and that the relationship with Delaware is of great importance to Credit Suisse.

Mr. Lane presents an analysis of Delaware's portfolio as of Monday, February, 23<sup>rd</sup> 2015. Mr. Lane states that the portfolio is currently overweight in the reserve due to some recent draws from liquidity. Mr. Lane states that this is a typical seasonal low and that new inflows will push the reserve account back towards the required fifty-fifty split between reserve and liquidity. Mr. Lane states that the portfolio has very little interest rate risk and that the fall in energy prices at the end of 2014 sent a few ripples through the credit markets.

Mr. Marvin notes that the down side of this credit risk may have been greater had the guidelines allowed single A purchases.

Mr. Lane agrees this is possible depending on sector selections. Mr. Lane notes that the managers like the increase flexibility that the Cash Management and Policy Board's revised guidelines allow and the allowance of single A's really puts a focus on the ability to analyze credit. Mr. Lane notes that concerns about Eurozone stability and the investment effects of cheaper energy prices benefitted Delaware's portfolio tremendously in January. Mr. Lane states that managers are using access to a broader list of international government bonds the Cash Management and Policy Board made available to gain yield differential versus U.S. bonds.

Mr. Lane notes that we are late in the economic cycle and suggests there may be some headwinds for economic growth in recent data. Wage growth in particular is absent and that recent strength can be seen in the United States but that this strength has dissipated in recent months. Mr. Lane notes that China continues to weaken and high quality Euro bonds are doing particularly well. Mr. Lane states that the Fed's extraordinary balance sheet creates an environment set for short run volatility, but that inflation is exceptionally low nationally and slightly faster regionally around Delaware.

Mr. Lane states that Fed watching will be a crucial in the near term and that as interest rate increases begin Credit Suisse expects a return to typical volatility in the six to twenty-four month portion of the yield curve. Mr. Lane states managers are bar belled around this portion of the yield curve, especially in the two-year portion. Mr. Lane states that a thorough analysis of the portfolio construct will be important going forward, but that protecting the stability of the portfolio in the face of volatility should garner equal consideration. Mr. Lane states that section four exemplifies the process Credit Suisse uses to provide a 30,000 foot picture of the portfolio.

Mr. Karia asks about a prior chart demonstrating maturity versus expected return which was not in the current presentation.

Mr. Lane states this can be provided.

Mr. Karia states that what he is looking for should be broken out by investment manager.

Mr. Black notes that page 17 has expected change in short term interest rates by manager.

Mr. Lane states that this is interest rate projections for the various global central banks but that Credit Suisse will provide the projections.

Mr. Simpler states his belief that we are exiting one weird financial period and entering a different weird period, but that a thoughtful, active policy analysis will be pivotal at this time. Mr. Simpler notes that the Cash Management and Policy Board must make sure that the policy guidelines are not meaningfully undermining the performance of managers. Mr. Simpler states that the Office of the State Treasurer hopes to meet with all the managers by the end of March and cautions about the long lag between deciding upon guideline changes and enacting them. Mr. Simpler hopes to understand the value the Cash Management and Policy Board has derived from its relationship with Credit Suisse in order to think critically about the value added by the independent advisor. Mr. Simpler asks for Credit Suisse's perceptions of their value add.

Mr. Marvin states that Mr. Simpler's comment is one of the more intelligent things said by a Treasurer in his thirty plus years on the Cash Management and Policy Board.

Mr. Lane notes that it is unfortunate that too much of Credit Suisse's historical work has not been visible for the Cash Management and Policy Board. Mr. Lane states that Credit Suisse's value add comes in terms of portfolio construct, strategy, and accountability to said strategy. Mr. Lane states that Credit Suisse measures the collective stewardship of Delaware's funds.

Mr. Jaffè notes that Credit Suisse has 48,000 employees around the world that enables the provision of a well-informed view in an advisory capacity. Mr. Jaffè states that Credit Suisse's global organization enables the company to provide better insight in a world where things that happen in one country effect many countries.

Mr. Chip Kurtzman, Director at Credit Suisse, notes that the recent development of Credit Suisse's quarterly conference calls with all the invest managers is an additional value the company provides.

Mr. Black states that to stay within accordance with the Freedom of Information Act someone should move to have the meeting go into executive session. Mr. Black states that the purpose for doing this is to keep the minutes of the executive session separate from the public session and would be exempt from FOIA until the reason for privacy has passed.

Mr. Flynn moves that the Cash Management and Policy Board go into executive session, Mr. Karia seconds, and the motion passes unopposed.

## **8. Investment Advisor Discussion**

Mr. Simpler recommends the Cash Management and Policy Board seeks a third party consultant. Mr. Simpler states that the Office of the State Treasurer will bring a proposal to the Investment Subcommittee and eventually the full Cash Management and Policy Board concerning the scope of services for the advisor position and that an RFP would be completed during this calendar year. Mr. Simpler states that as a bridge during this process the Office of the State Treasurer will reach out to Credit Suisse and attempt to retain their service until the RFP can be completed. Mr. Simpler states that the scope of service will be defined and presented to the Investment Subcommittee in the next 30 to 45 days including feedback provided by investment managers.

Mr. Flynn asks if there is any further investment discussion and there is none.

#### **9. Future Meetings and Agenda**

Mr. Flynn asks if meetings should be held quarterly in the future.

Mr. Simpler states that meeting shortly after quarterly performance reports seems to make sense. Mr. Simpler asks if requirements that the Cash Management and Policy Board meet four times a year refers to a fiscal year or a calendar year.

Mr. Black states that the legislative requirement is for the fiscal year and that the Cash Management and Policy Board should meet twice more prior to June 30<sup>th</sup>.

Mr. Marvin states that the Cash Management and Policy Board should plan on some meetings being telephonic in advance.

Mr. Simpler states that the Office of the State Treasurer would be happy to forward a proposed meeting schedule for the next 18 months.

Mr. Flynn states that he and Mr. Simpler will confer on a schedule and plan to have another meeting in April regarding the recommendations from the Investment Subcommittee on the scope of services for the advisor role and then having a final Cash Management and Policy Board meeting towards the end of the fiscal year.

Mr. Simpler states that the meeting in April might also include a list of the proposals from investment managers that could be acted upon.

#### **10. New Business**

Mr. Flynn asks if there is any new business and there is none.

#### **11. Public Comment**

Mr. Flynn asks if there is any public comment and there is none.

#### **12. Adjournment**

The meeting was adjourned.