Banking Services RFP Preparation, Evaluation, and Hot Tips

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Maria Altomare, a Managing Director in the St. Louis Missouri office, joined PFM in January 2006. Ms. Altomare assists public entities in Missouri, Nebraska, Wyoming and Kansas with cash management services, including the marketing of individual portfolios, investment pools, fixed income products and bond proceeds investment. In addition, Ms. Altomare serves as a national sales representative for purchasing card products and services. She prides herself in providing her clients with excellent customer service. Prior to joining PFM, Ms. Altomare had over 20 years experience in the banking industry. Her roles included Vice President, Government Banking Division at U.S. Bank; N.A, Head of Corporate Cash Management for Allied Irish Bank, Dublin, Ireland; and she spent 15 years with the Canadian Imperial Bank of Commerce "CIBC" mainly in management roles in business development and customer service for credit, investments, cash management, and credit card services. In 1991, Ms. Altomare completed a two-year certificate in banking at York University, Toronto, Canada and received her letter of accomplishment from the Institute of Canadian Bankers Association. In addition to her work experience, Ms. Altomare holds NASD Exams: Series 6 and 63.
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I. Introduction to PFM
Firm Overview

PFM Asset Management LLC

- Fixed-Income Portfolio Management
- Bond Proceeds Management
- Arbitrage Rebate Compliance

Investment Consulting
- Treasury Management Consulting
- Multi-Asset Class Advisors

Public Financial Management, Inc.

- Financial Advisor
- Debt Management
- Strategic Planning Services
Company Profile

- PFMAM is registered with the SEC under the Investment Advisors Act of 1940
- Over $40 billion of public assets under management nationwide\(^1\)

National perspective

- 33 offices nationwide
- Over 440 financial professionals working with the public sector
- Regional office in St. Louis, Missouri

Treasury Consulting Services

- Providing banking and treasury consulting services since 1989
- Independent; not affiliated with any bank or trust company
- Our objective is to ensure that clients get the best banking service at the best cost
- Consulting fees are nominal compared to savings typically realized

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1. As of June 30, 2011
3. Pension & Investments 2010 Survey of Top Money Managers ranked by U.S. institutional tax-exempt assets managed internally
II. The RFP Process
RFP Process Introduction

• The right bank relationship can make a world of difference in day-to-day treasury operations, and traditionally, a Request for Proposal (RFP) has been the method to confidently and objectively select a banking partner.

A 5 Step Approach to Finding the Right Bank

1. Document the Current Environment
   • “Where are we now?”

2. Develop the RFP
   • “What services do we want our bank to provide?”

3. Evaluate the Bank Responses
   • “How do the banks say they measure up to your requirements?”

4. Bank Presentations and Visits
   • “Can the banks really deliver what you require?”

5. Selection & Implementation Plan
   • “What are the specific next steps?”
Step 1. Document Current Environment

• Ask your banks for an Account Analysis statement for each account and document;
  ➢ what services you currently use
  ➢ what are your volumes
  ➢ how much do you pay
  ➢ how does the money move.

• Design a checklist determining necessary information to gather from each internal department and the services they may require

• Identify areas of improvement through use of technology
5 Step Approach to Finding the Right Bank

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Step 2. Develop the RFP

Prepare the RFP based on your school's needs.

- **Content of RFP:**
  A. General Information about your school
  B. Calendar of Events
  C. Minimum Proposal Requirements
  D. Scope of Services
  E. Questions and Requested Information
  F. Special Contract Provisions
  G. Q&A

- Email RFP in a word document to all banks

Tip: Through new innovative ideas allow potential banks the opportunity to show how and why they should be your partner.
A. General Information About Your School

- Description of your school
- Contact name
- Submission instructions
  - Sealed Proposal
  - Mailing Information
  - Number of Copies
  - Request addendums, reports, contracts etc
- Any special requests (reasonable)

Tip: Describing who you are is just as important as identifying what services you need. If the banks don’t realize the scope of your potential business you won’t get a reasonable response.
B. Calendar of Events

- Issue date
- Deadline for written questions
- Pre-proposal conference (for larger schools)
- Proposal due date
- Interviews
- Contract approval
- Contract implementation

Tip: Allow adequate response time (4-6 weeks).
C. Minimum Proposer Requirements

• Size
• Location
• Experience
• Organizational structure
• Community Reinvestment Act (CRA)
• Community involvement
• Credit rating of the bank
• FDIC Insurance Risk Category of the bank
• Request the index rate you want the banks to bid (91 day t-bill, fed funds, etc.)
• If banks bid different rate than requested, ask for 2 years of history comparison to what has been requested

Tip: Risk Categories go from 1-4 with the 4 paying the highest FDIC insurance.
D. Scope of Services

- Term of agreement
- Account structure
- Collateral requirements
- Average monthly balances
- Required and optional services
- Pricing excel sheet with monthly or annual volumes

Tip: Be sure to state that investments maybe bid outside of the banking contract and collateral must follow Missouri State Statue.
E. Questions and Requested Information

- Keep questions short and concise to drive easy answers for your review.
- Request a sample Account Analysis Statement
- Request different Availability schedules
- List any other documents you may want to review such as:
  - Contracts
  - Account open forms
  - Treasury Management Agreements
  - Individual service agreements (wires, ACH)
  - Let the banks know if only the finalists will need to submit these documents

Tip: If you use an RFP that another school used be sure to review all the questions to ensure they match the banking services that your school needs.
F. Special Contract Provisions

- Timely contract negotiations
- Failure to comply with provisions
- Proof of insurance
- Dispute resolution
- Data privacy
- Affirmative action
- Termination

Tip: Be sure to state that the RFP Proposal submitted is considered the final contract and must be signed by an authorized signor of the bank.
G. Q & A

• Require questions in writing
• Set submission deadline
• Provide written answers
• No need to answer all questions

Tip: Break services into sections, Banking, Procurement Card, Merchant Services and state if they can bid on one or all sections.
5 Step Approach to Finding the Right Bank

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Step 3. Evaluate the Bank Responses

- Evaluate responses in terms of:
  - Operational capabilities
  - Experience and Staff
  - Financial strength
  - Financial controls
  - Location, location, location
  - Quality of Proposal
  - Creative or new approaches
  - Evaluate Fees and Earnings

Tip: Be open minded to new ideas on how to automate your banking and protect your school district from fraud.
Evaluation Criteria

- Operational capabilities
  - Existing services
  - New services
  - Available platforms
  - Cut-off times
  - Availability schedule

- Experience and Staff
  - Customer service structure
  - People
  - Community involvement
Evaluation Criteria

• Financial strength
  ➢ Financial statements
  ➢ Ratings
  ➢ FDIC Insurance Risk Category

• Financial controls
  ➢ Disaster recovery
  ➢ Online systems and data security

• Location, location, location
  ➢ Number of branches
  ➢ Proximity to operations
  ➢ Lockbox address
Evaluation Criteria

• Quality of Proposal
  ➢ Understand your business
  ➢ Attention to detail
  ➢ Want your business

• Creative or new approaches
  ➢ New payment and collection devices
  ➢ Automated reporting
  ➢ Employee benefits
  ➢ “Other” services
Evaluation - Fees

• Fee Proposal
  ➢ Bundled or unbundled
  ➢ Volume levels
  ➢ Maintenance and usage

• AFP (TMA) Service Codes

• FDIC Charges

• Collateral Charges

• Trust & Custody Fees

• Fee Waivers

• Other fees?
Evaluation - Earnings

• Investment earnings
  ➢ Account type
  ➢ Historic rates
  ➢ Sweep fees

• Earnings Credit Rate
  ➢ Index based?
  ➢ Excess earnings (carried forward or not?)

• Reserve Requirement

Tip: Repurchase agreements are included in balances for FDIC Insurance costs.
## Evaluation of Banking Services Proposals

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<td>Location (e.g. branches, operations center, account officers)</td>
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<td>Experience, resources, and qualifications of institution and assigned staff</td>
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<td>Relevant experience managing similar account relationships with public institutions and agency clients</td>
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<td>Financial Strength</td>
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<td>The value of any new product or service suggestions or other new ideas and enhancements</td>
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<td>Compliance with the requirements of the RFP, completeness and quality of proposal</td>
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<td>TOTAL SCORE</td>
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<td>100</td>
<td>100</td>
<td>75</td>
<td>100</td>
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Step 4. Bank Presentations and Visits

• Shortlist by eliminating bidders
  ➢ Must meet minimum requirements
  ➢ Must offer necessary services
  ➢ Must demonstrate service capability
  ➢ Attention to detail

• Interview real contenders
  ➢ Request key staff
  ➢ Define presentation content
  ➢ Discuss all major service needs
  ➢ Understand fee proposal
  ➢ Allow enough time
Everything is Negotiable

- Fees
- Earnings rates
- Deposit availability
- Account coverage
- Contract terms
5 Step Approach to Finding the Right Bank

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   - “What are the specific next steps?”
Step 5. Selection & Implementation Plan

- Select the preferred bank(s)

- Develop overall implementation plan which includes:
  - Key project tasks and dependencies
  - Staffing and skill set requirements
  - Timeframes
  - Key deliverables
Don’t Forget…

• Incorporate RFP and the bank’s proposal
• Get copies of all referenced documents
• Document collateral requirements and any investment limitations
• Include the term and termination provisions
• Have lawyers check compliance with statutory requirements
• Confirm signed by authorized signer
• Confirm in writing the proposal is the final bid
• Maintain an open dialogue with your banking partners
• Monitor: Service, Error Rate, and Correct Billing

Tip: watch out for small print on account open forms.
Lock in the Fees and Rates

WATCH OUT FOR: “We reserve the right to amend from time to time the Account Fees for the Service without notice to you.”

- Tie earnings credit rate (ECR) and interest rate to index
- Document ECR carry forward
- Require written authorization for new services and charges

Tip: Be cautious of bids tied to LIBOR. This rate is very volatile.
Know Your Rights

WATCH OUT FOR: “Client is required to notify Bank of any errors within 10 days of the receipt of the Statement of Confirmation or the Bank is relieved of all liability related to the error.”

• The Uniform Commercial Code gives you certain legal rights
• Standard bank agreements often waive those rights
• Example
  ➢ UCC requires notice of error be made to the bank within a reasonable time, not to exceed 90 days.
Who’s Responsible for Security?

WATCH OUT FOR: “Client agrees that Bank’s security procedures for use of Service are reasonable based on Client’s circumstances.”

“The Bank shall during the term of this Agreement provide commercially reasonable security procedures considering the type of files processed and security procedures used by customers and banks similarly situated. The Client accepts the current security procedures offered by the Bank as commercially reasonable, but this shall not relieve the Bank of the continuing duty to maintain commercially reasonable security procedures during the term of this Agreement.”
III. Case Studies
Case Study #1 –
How Much Are You Really Earning?
How Much Are You Really Earning?

• Here’s an example of how typical bank fees can reduce a quoted rate of 0.30%. In this example, after all the assessments and hold-backs are considered, the actual net return is only 0.058%.

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<tr>
<th>Description</th>
<th>Balance/Charge</th>
<th>Earnings/Cost*</th>
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<tbody>
<tr>
<td>Ledger Balance</td>
<td>5,000,000</td>
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</tr>
<tr>
<td>FDIC Assessment</td>
<td>0.17%</td>
<td>($8,500)</td>
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<tr>
<td>Less: Check Float</td>
<td>1,000,000</td>
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<tr>
<td>Collected Balance</td>
<td>4,000,000</td>
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<tr>
<td>Less: 10% Reserve Requirement</td>
<td>(400,000)</td>
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<tr>
<td>Available Balance</td>
<td>3,600,000</td>
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<tr>
<td>Earnings at 0.30%</td>
<td>0.30%</td>
<td>$10,800</td>
</tr>
<tr>
<td>Net Return (on Collected Balance)</td>
<td>0.058%</td>
<td>$2,300</td>
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• *All fees and earnings annualized.

• What? How does that happen? Where did the 0.30% earnings rate go?
  ➢ Some of it goes to the FDIC and some of it goes to the bank
FDIC Assessments

- FDIC charges banks for deposit insurance
- April 1, 2011 change to assessments
  - Based on net assets instead of domestic deposits
  - Rates vary from 0.05% - 0.35%
  - FDIC assessments are paid on ledger balances
- Not all banks pass through FDIC assessments
- Banks that pass through assessments charge on either collected or ledger balance
- Fee shown on analysis statement
FDIC Assessments

- In our example, the FDIC Assessment fee of 0.17% of the ledger balance is passed through to the client, which comes out to $8,500 per year.
- For some banks, the FDIC Assessment fee is higher! (FDIC 0.12% to 0.22%)

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- *All fees and earnings are annualized*
**Less: Check Float**

- Although the FDIC assessment is based on your ledger balance, the earnings rate is based on your collected balance.
- For cities with check float, this can significantly reduce your net return on deposits.

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Reserve Requirements

• Depository institutions must hold funds in reserve at the Federal Reserve

• Reserve requirement varies by type of account
  - Demand deposit: 10%
  - NOW Account: 10%
  - Money market deposit: 0%
  - Time deposit: 0%

• In October 2008, the Fed began paying interest to banks on these balances

Source: Federal Reserve
Less: 10% Reserve Requirements

- Because these reserve balances are not available for loans or investment, banks have generally not paid depositors interest on amounts that must be reserved.
- This means that the depositor only earned income on 90% of the balance.

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Summary of Case Study #1

- After adjusting for all of these assessments and hold-backs, the actual earnings per year on this $5,000,000 account actually comes out to $2,300, resulting in a net return of just 0.058% - well below the quoted 0.30% rate.

- **The bottom line**: You may not be getting quite the “deal” you expected from your bank after adjusting for all the potential assessments and hold-backs.

- The only way to tell if you’re really getting a great deal from your bank is to carefully review your bank account analysis statement. If you’re not currently receiving a bank account analysis statement every month, request it from your banker.
Case Study #2 – Compensating Balances
Case Study # 2 – Compensating Balances

• If you’ve ever had a discussion with your banker regarding fees for services, you’ve likely heard the term “compensating balance” mentioned a few times.

• So, you might be wondering, “Just what is a compensating balance and what do I need to know about it?”,

• We’ll look at what exactly a compensating balance is and how to make sure that you are getting a fair deal.
Two Options to Pay for Banking Services

1) Out of pocket fee that is charged to your city each month as an invoiced item. The invoice is paid like any other accounts payable. This method of compensation is called “hard dollars”.

2) “Pay” by using compensating balances
   - A compensating balance is money left in a bank account on which the city is not paid interest.
   - Instead, an “earnings credit” is generated that is used to pay for bank fees. The amount of the earnings credit is a function of the un-invested balance and an Earnings Credit Rate (“ECR”). This method of compensating your bank is also called “soft dollars”.

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Determining Compensating Balances

• Typically, your banker will look at your historical account activity to determine an average monthly fee for service.

• He or she will then quote the current Earnings Credit Rate available, before performing a quick calculation to determine the amount your city will need to keep on deposit at the bank in order to offset banking fees.

• The discussion might sound something like this: “We’ll give you a 1.00% Earnings Credit Rate on the amount you have on deposit with us. You are typically charged about $10,000 per month in banking fees, so in order to offset this fee with no out-of-pocket fees for our services, you will need to keep a compensating balance of at least $1 million with our bank.”
Impact of Rising Rates

Balance Needed to Cover
$10,000 of Banking Fees

Compensating Balance

- $1,000,000
- $800,000
- $600,000
- $400,000
- $200,000
- $-

Earnings Credit Rate

- 1.00% ECR
  - $1,000,000
- 4.50% ECR
  - $250,000

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Compensating Balance Gotchas

- Excess earnings credits
- No roll forward of excess earnings credit
- Application of 10% reserve requirement
- Temporary “special” ECR
- Unneeded services
- Full list prices on services
- Fixed compensating balance
Summary of Case Study #2

• **The bottom line**: Choosing to “pay” for banking service fees using a compensating balance may or may not be a good option for your city.

• The only way to tell if you’re really getting a great deal from your bank is to carefully review your bank account analysis statement. If you’re not currently receiving a bank analysis statement every month, request it from your banker.
Case Study #3 – Everything is Negotiable!
Case Study# 3 – Everything is Negotiable!

- After the first two case studies, you may be thinking, “Hmm . . . interesting stuff, but I don’t think any of this really affects me. After all, my school is locked into a banking arrangement. We even signed a contract, so I don’t think I’m in a position to try to press my banker for a better deal.” Well, you might be wrong about that.

- Actually, when it comes to banking service arrangements, the truth is that everything is negotiable.
Negotiable Areas to Achieve Better Pricing

- Availability Schedule
- Banking Fees
- Start-up Fees for New Services
Concessions for Better Pricing?

• Yes, you probably will have to make some concessions. Here are a few areas in which you could make those concessions without feeling the pinch too much:

  ➢ Contract Extension
  ➢ New Business
Summary of Case Study#3

• **The bottom line**: When it comes to business banking, everything is negotiable. If you don’t think that you’re getting the best deal from your bank, contact your banker directly and ask for a better deal. Most likely, he or she will be willing to acquiesce to your terms rather than lose your business.

• However, if your banker does seem unwilling to offer the fee concessions or service upgrades you’d like, contact other banks to see what they would offer. There are a lot of banks out there who would love to do business with your entity, so make your current banker work to keep your business.

• PFM has helped dozens of clients to analyze their banking relationships, negotiate for better terms, or go through a competitive banking services procurement process. If you don’t believe you are getting the right service, you can always bid out banking services.
Appendix
Glossary of Banking Terms

Account Analysis Terminology:

Account Analysis Statement - a periodic statement outlining the banking services provided to your entity. The statement is usually provided monthly and involves displaying all pertinent data, including the company’s average daily balance and charges that the company incurs from the bank.

Ledger Balance – Customer’s account balance as it appears on a bank statement. The sole purpose of ledger balances, or total credits less debts during an accounting period, is to facilitate the reconciliation of book balances. Does not include float.

Available Balance – represents total funds as available for use.

Collected balance – cash balance after deducting checks drawn on other banks. Generally defined as account ledger balances, less unpaid checks in the process of collection. A bank may count a deposited check as funds available for use by its customer in two business days, but usually will not include it in the depositor’s collected balance for five or six days. This allows time for the drawer bank to return the check because of insufficient funds in the check maker’s account or for other reasons. Ledger balance less float.

DDA balance used to offset fees is a Compensating Balance. Also known as “soft dollars”

Deposit Float – “in process” deposit items. Waiting period for collected funds.

Earnings Credit Rate (ECR) - Typically a variable rate and usually equal to the average rate on 91-day Treasury Bills or Fed Funds Target rate.
**Basis Point** - One one-hundredth of a percent used in measuring yield differences among bonds. A rise from 5.41% to 5.61% would be termed a rise of 20 basis points.

**Daily Treasury Bill Rates** - These rates are the daily secondary market quotation on the most recently auctioned Treasury Bills for each maturity tranche (4-week, 13-week, 26-week, and 52-week) that Treasury currently issues new Bills. Market quotations are obtained at approximately 3:30 PM each business day by the Federal Reserve Bank of New York.

**Federal funds rate** - the interest rate at which private depository institutions (mostly banks) lend balances (federal funds) at the Federal Reserve to other depository institutions, usually overnight. It is the interest rate banks charge each other for loans.

**Federal funds effective rate** - the interest rate that the borrowing bank pays to the lending bank to borrow the funds is negotiated between the two banks, and the weighted average of this rate across all such transactions.

**Federal funds target rate** - determined by a meeting of the members of the Federal Open Market Committee which normally occurs eight times a year about seven weeks apart. The committee may also hold additional meetings and implement target rate changes outside of its normal schedule.

**LIBOR** - the interest rate that banks charge each other for one-month, three-month, six-month and one-year loans. LIBOR is an acronym for London InterBank Offered Rate. This rate is that which is charged by London banks, and is then published and used as the benchmark for bank rates all over the world. LIBOR is compiled by the British Bankers Association (BBA), and is published 11 am each day in conjunction with Reuters. It is comprised from a panel of banks representing countries in each currency.
Review of Tips

• Through new innovative ideas allow potential banks the opportunity to show how and why they should be your partner.
• Describing who you are is just as important as identifying what services you need. If the banks don’t realize the scope of your potential business you won’t get a reasonable response.
• Allow adequate response time (4-6 weeks).
• Risk Categories go from 1-4 with the 4 paying the highest FDIC insurance.
• Be sure to state that investments maybe bid outside of the banking contract and collateral must follow Missouri State Statue.
• If you use an RFP that another school used be sure to review all the questions to ensure they match the banking services that your school needs.
• Be sure to state that the RFP Proposal submitted is considered the final contract and must be signed by an authorized signor of the bank.
• Break services into sections, Banking, Procurement Card, Merchant Services and state if they may bid on one or all sections.
• Be open minded to new ideas on how to automate your banking and protect your school district from fraud.
• Repurchase agreements are included in balances for FDIC Insurance costs.
• Watch out for small print on account open forms.
• Be cautious of bids tied to LIBOR. This rate is very volatile.
Earnings Credit Calculation

Example:

- Average collected balance
  $1,900,000
- Reserve requirement  10%
- Earning credit rate  3.00%
- Days in month  31

\[
\text{Earnings Credit} = \text{Collected Balance} \times \left[ 1 - \text{Reserve Requirement} \right] \times \left[ \frac{\text{Earnings Credit Rate}}{365} \right] \times \text{Days in Month}
\]

\[
\text{Earnings Credit} = $1,900,000 \times \left[ 1 - .10 \right] \times \left[ .03 \times \frac{31}{365} \right]
\]

\[
= $1,900,000 \times .90 \times .0025479
\]

\[
= $4,356.99
\]
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