



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

SUBJECT: REPORT ON RFP
BANKING AND FINANCIAL
SERVICES

FROM: Julia H. Cooper

DATE: April 15, 2009

Approved

Christine J. Shippin

Date

4/20/09

COUNCIL DISTRICT: Citywide

RECOMMENDATION

- (a) Adopt a resolution to authorize the City Manager and the City Manager's authorized designees ("City Manager") to:
- (1) Negotiate and execute agreements with Wells Fargo Bank, N.A. (the "Bank") for banking and financial services including General Banking Services, Merchant Card Processing Services and Lockbox Services for an initial term commencing with the execution of the agreements by the parties through June 30, 2012; and Securities Custody Services for an initial term of July 1, 2009 to June 30, 2012, with a total maximum annual compensation for the four agreements for the period through June 30, 2010 not to exceed \$864,000 and, thereafter, subject to annual appropriation of funds for the second and third year of the initial term.
 - (2) Execute up to three additional two-year options for one or more of each of the four agreements subject to annual appropriation of funds.
 - (3) Negotiate and execute amendments to any of the four agreements with the Bank, subject to annual appropriation of funds by the City Council and the parameters specified in the resolution to: (a) add new banking and financial services, (b) revise the descriptions of the banking and financial services; and (c) increase the compensation paid to the Bank if the volume of services exceeds the estimated volume of services.
 - (b) Adopt a resolution authorizing the City Manager to negotiate and execute an agreement with Union Bank of California ("UBOC") to provide final banking services related to the City's Commercial Account, Lockbox and Merchant Card services for the period of July 1, 2009 to June 30, 2010 in an amount not to exceed \$30,000.

OUTCOME

Approval of this recommendation will allow the City to enter into agreements for a variety of banking services with Wells Fargo Bank allowing for enhanced services at a reduced cost for the City's extensive banking operations. In addition, a recommendation to enter into a one-year agreement with Union Bank of California to provide limited banking services related to the processing and payment of checks issued by the City that are still outstanding.

EXECUTIVE SUMMARY

The recommendations contained in this memorandum include authorization for the City Manager to negotiate and execute agreements with Wells Fargo Bank, N.A. for providing banking services to the City of San Jose for the initial term commencing with the execution of the agreements through June 30, 2012 with three two-year options for extending the agreements at the City's sole discretion. The banking services included in the agreements includes general banking services, merchant card processing services, lockbox services and security custody services. The report describes the request for proposal evaluation process, the terms and conditions of the agreements and services to be provided under the agreements.

BACKGROUND

The last Request for Proposals for banking services was conducted in 1999 with City Council approval of the Agreement with Union Bank of California to provide general banking services in March 2000. The eighth amendment to the Agreement with UBOC was approved by the City Council on March 24, 2009. While the expiration date of the original agreement including the extension terms was 2005, additional extensions were approved by the City Council. These extensions relied on the original competitive process as the basis for the extension. The Request for Proposal process for banking services was delayed over the last several years due to other competing Council priorities, staffing turn-over, and the resulting vacancies.

ANALYSIS

This section of the report is divided into five sections:

- Discussion of the current state of the financial and banking service sector.
- Participation of the Redevelopment Agency in the RFP process.
- Discussion of the RFP and evaluation summary.
- Implementation plan, including overlap services with Union Bank of California.
- Summarization of the terms and conditions for the agreements with Wells Fargo Bank.

Current State of Financial and Banking Service Sector

Since commencement of the City's RFP process for General Banking Services, the world's financial institutions have experienced significant challenges. Credit related losses worldwide currently stand at approximately \$1.3 trillion. The Federal Deposit Insurance Corporation's (FDIC) Quarterly Banking Profile reported a net loss of \$32.1 billion at insured commercial banks and savings institutions for the fourth quarter 2008. This represents the industry's first aggregate quarterly loss since 1990.

In response to the financial turmoil, the United States Government has identified the banking system as a primary driver of future economic growth. The focused attention on the banking system is demonstrated by a recent Joint Statement by the US Treasury, FDIC and the Federal Reserve on February 23, 2009 that stated, "*The US government stands firmly behind the banking system during this period of financial strain to ensure it will be able to perform its key function of providing credit to households and businesses. The government will ensure that banks have the capital and liquidity they need to provide the credit necessary to restore economic growth.*"

To ensure the banking sector provides a pivotal role in elevating the nation out of recession, the US Treasury, FDIC, and the Federal Reserve, have implemented several programs to help stabilize and strengthen the nation's financial system. To date, the government has directly injected approximately \$300 billion into over 400 of the nation's financial institutions through the Troubled Asset Relief Program (TARP). The Capital Purchase Program, a part of TARP, is authorized to invest an additional \$250 billion into the nation's largest financial institutions based on the outcome of forward looking capital assessments of the institutions. In addition, the government has created vehicles to support markets that financial institutions rely on for their ongoing funding needs including: commercial paper, corporate notes and money markets.

Wells Fargo Bank N.A.: Wells Fargo & Company, whose principal subsidiary is Wells Fargo Bank N.A., is the oldest and largest bank holding company headquartered in California. Wells Fargo & Company is a diversified financial services company with \$1.3 trillion in assets that provides banking, insurance, investments, mortgage and consumer finance through more than 11,000 stores, over 12,000 ATMs and via the internet across North America and internationally.

On October 28, 2008 Wells Fargo was one of nine financial institutions asked by the Treasury Department to accept TARP funding, through the Capital Purchase Program, to restore confidence in the US financial sector. Wells Fargo received a \$25 billion dollar direct investment and has not accepted any further assistance as of April 10, 2009. Wells Fargo acquired Wachovia Bank during 2008 with the acquisition successfully closing on December 3, 2008. The merger between Wells Fargo and Wachovia creates the second largest deposit-taking institution in the country.

Wells Fargo Bank was one of the last financial institutions in the US to retain a AAA credit rating, but due to continued stresses in the housing market and write downs associated with the merger of Wachovia, both Moody's and Standard & Poor's placed Wells Fargo's credit ratings outlook on negative watch status. Moody's completed its review of Wells Fargo Bank on March

25, 2009 and lowered its ratings on Wells Fargo Bank one notch from Aa1 to Aa2. In addition, Moody's reinstated a "stable" outlook for Wells Fargo, which implies no further rating changes are anticipated in the near term. As of April 10, 2009, Standard & Poor's has not taken any rating action concerning their negative outlook.

Table 1
WELLS FARGO BANK RATINGS
as of April 10, 2009

	<u>Moody's¹</u>	<u>Standard & Poor's²</u>	<u>Fitch Ratings³</u>
Ratings Outlook	Stable	Negative	Stable
Long-term Issuer Rating	Aa2	AA+	AA
Long-term Bank Deposits	Aa2	Not Rated	AA+

¹ Last update March 25, 2009

² Last update December 19, 2008

³ Last update November 6, 2007

Redevelopment Agency's Participation in RFP Process

The RFP included the possibility of incorporating the Redevelopment Agency's banking services with the City's banking services. As part of the RFP process, Redevelopment Agency staff participated in the development of the RFP and review of the RFP responses. The Agency has elected to maintain their existing banking relationship with Bank of America and they will not be consolidating their banking relationship with the City's banking services.

Request for Proposal Process and Evaluation Summary

A Request for Proposal (RFP) for Financial Services, which included the City's General Banking Services, Lockbox Services, Merchant Card Processing, and Securities Custody services, was issued through the City's e-procurement system on February 28, 2008 and eight companies were directly notified. Through the City's e-procurement system a total of 36 companies viewed the requirements and seven companies submitted proposals for one, or all, of the services by the May 30, 2008 due date. The respondents included:

- Bank of America
- Bank of the West
- Comerica
- JP Morgan Chase
- Union Bank of California
- US Bank
- Wells Fargo

The proposals were reviewed and evaluated utilizing several different methods (minimum qualifications and technical review that are described below).

Minimum Qualifications: The initial proposal review consisted of a pass/fail assessment to ensure that all minimum qualifications were met and that all proposals were complete. All proposals were found to be responsive.

Evaluation Team: An eight-member evaluation panel was named with representatives from the Finance Department, the Redevelopment Agency, and the Parks, Recreation and Neighborhood Services Department. The Informational Technology Department also participated as a consultant to the evaluation team on Procurement Card Industry (PCI) standards and technology enhancements. A representative from the Finance Department's Purchasing Division facilitated all team meetings.

Technical Evaluation: The technical evaluation consisted of a thorough review of each company's written proposal for technical capability, experience, product functionality and demonstrated experience implementing banking services similar in size and complexity to the City's requirements, and technological enhancements to improve the City's financial management operations. The written evaluations were followed by oral presentations/interviews. Technical scores were initially determined after the written proposals were evaluated and finalized after oral presentations.

Cost Proposal: Proposers were asked to provide a fee structure for each of the four services groups that their Company proposed based on the City's current monthly actual volumes in each group. This fee structure was used to evaluate the cost score.

Oral Interview/Presentations: The evaluation team determined that four Proposers earned scores in the competitive range and were invited for oral interview/presentations. Comerica Bank, Bank of the West and Union Bank were not considered for further evaluation due to low technical scores. All Proposers were notified of the City's decision, offered a debriefing, and provided the opportunity to protest the decision to the City's Chief Purchasing Officer. The City held two debriefings, one with Union Bank and the other with Comerica Bank. The companies did not protest the City's decision.

Oral Interview/Presentations were held on September 3rd, 4th, and 5th, of 2008 to clarify responses to the RFP, demonstrate Proposers' knowledge and ability to meet the City's requirements, and to meet key personnel that would make up the implementation team who would be assigned to the City's accounts. Technical scores were finalized upon completion of the oral presentations. All Proposers were notified of the City's decision to recommend Wells Fargo for award of contract and offered a debriefing. The City held two debriefings with US Bank and JP Morgan Chase.

Final scores and ranks are summarized in the following four tables for distinct services:

Table 2
CITY OF SAN JOSE – REQUEST FOR PROPOSAL BANKING SERVICES
GENERAL BANKING SERVICES EVALUATION

Rating Criteria	Maximum Points	Wells Fargo Bank	US Bank	Bank of America
Experience	35	32	29	25
Technical	40	37	34	34
Cost	15	15	14	13
Local Business ...	5	0	5	5
Small Business ...	5	0	0	0
TOTAL	100	85	82	77

Table 3
CITY OF SAN JOSE – REQUEST FOR PROPOSAL BANKING SERVICES
LOCK BOX SERVICES EVALUATION

Rating Criteria	Maximum Points	Wells Fargo Bank	US Bank	Bank of America
Experience	35	32	29	25
Technical	40	35	25	26
Cost	15	6	9	15
Local Business ...	5	0	5	5
Small Business ...	5	0	0	0
TOTAL	100	74	67	71

Table 4
CITY OF SAN JOSE – REQUEST FOR PROPOSAL BANKING SERVICES
SECURITIES CUSTODY SERVICES EVALUATION

Rating Criteria	Maximum Points	Wells Fargo Bank	US Bank
Experience	35	32	29
Technical	40	34	32
Cost	15	9	2
Local Business ...	5	0	5
Small Business ...	5	0	0
TOTAL	100	75	68

Table 5
CITY OF SAN JOSE – REQUEST FOR PROPOSAL BANKING SERVICES
MERCHANT CARD SERVICES EVALUATION

Rating Criteria:	Maximum Points	Wells Fargo Bank	US Bank	Bank of America	JP Morgan Chase
Experience	35	32	29	25	21
Technical	40	24	23	24	31
Cost	15	15	14	15	15
Local Business....	5	0	5	5	0
Small Business ...	5	0	0	0	0
TOTAL	100	71	71	69	67

Local and Small Business Preference: In accordance with City policy, ten percent of the total possible evaluation points were reserved for local and small business preference. Three Proposers requested consideration for the City's local business preference. The application of the local business preference had no effect on the recommendation of award.

Protest Period: The City's RFP process provides the opportunity for unsuccessful proposers to protest the City's award recommendation. The Chief Purchasing Officer (CPO) received no protests.

Recommendation: Based on the evaluation process, staff has determined that Wells Fargo submitted the most overall advantageous proposal for all four financial/banking services. By having all four financial/banking services with one bank, the City will realize an overall cost

savings in staff time, training and a synergy with one bank that has an expertise in all the City's banking services.

Wells Fargo has a proven track record of successful implementations and a superior customer service team. Before recent financial sector turmoil, Wells Fargo was the only bank in the US, and one of only two banks worldwide, to have received the highest possible credit rating from Moody's (Aaa) and Standard & Poor's Rating Services of (AAA). There are currently no banks rated AAA in the US or in the world. Wells Fargo is currently one of the highest rated banks in the country with Aa2 and AA+ ratings from Moody's and Standard & Poor's, respectively. Moreover, Wells Fargo was also rated "Outstanding" for Community Reinvestment Act Performance by the Office of the Comptroller of the Currency, and is the number one purchaser of renewable energy in the US as confirmed by the Environmental Protection Agency. Wells Fargo and its merchant card providers are certified in the latest PCI-DSS and PA-DSS standards. In addition, Wells Fargo is the only national bank headquartered in California and is a recognized technology leader in its field. All of these elements support staff's recommendation.

Implementation Plan and UBOC Overlap Services

The City and Wells Fargo will commence formal transition of three of the four financial services after City Council approval and execution of the agreement, estimated to be on or about May 15, 2009. Wells Fargo Bank currently provides the City with security custody services, therefore no transition is involved. Wells Fargo will continue to provide the same security custody services, but under the new Agreement commencing July 1, 2009. Wells Fargo will require approximately 120 days to complete the entire implementation of the transition of the City's banking services. The table below provides the estimated date of conversion from Union Bank of California to Wells Fargo Bank for the three impacted banking service areas.

Table 6
BANKING SERVICES TRANSITION SCHEDULE

	<u>Estimated Transition Dates</u>
General Banking	June 1 – July 31, 2009
Merchant Card	July 1, 2009
Lockbox	September 1, 2009
Securities/Custody	July 1, 2009*

** No transition required; effective date of new Agreement*

The time between the start date of the formal Agreements in May 2009 and the various conversion dates is required to accomplish a number of pre-conversion activities including, but not limited to, the following:

- Establish numerous (approximately 27) City accounts.
- Set up the City's online banking with Wells Fargo.
- Create the interface with the City's various billing systems in coordination with the City's Information Technology staff.
- Test and set up all payroll and workers' compensation accounts and various disbursements.
- Establish desktop deposit for approximately 55 users.
- Initiate all merchant identification numbers and terminals throughout the City for credit card acceptance.
- Develop the City signatory information in plates and digital format.
- Design and print all forms needed for City's banking services.
- Train City staff on new technologies and systems offered by Wells Fargo Bank.
- Coordinate all processes with the City's Project Manager to have all products and services tested and in place by appropriate conversion dates.

During the conversion periods it will be necessary to retain the services of UBOC. Additionally, the City is required to maintain an account at UBOC for a period not less than six months from the time the last check is issued against the UBOC account to allow customers sufficient time to cash the check. The City is proposing to have this time period extended approximately 12 months (until June 30, 2010) to provide a "cushion" for our customers. Furthermore, staff will closely monitor the number (quantity) and dollar amount of the checks outstanding along with the costs of keeping the account open past the six month requirement. Depending on these variables, staff may elect to terminate the account and agreement with UBOC prior to June 30, 2010 upon providing 30 days notice to UBOC. In addition, Lockbox services will be maintained for approximately three months to collect payments and transfer the mail to the Wells Fargo Lockbox for processing. This will allow sufficient time for customer notification of the change.

Summary of Terms and Conditions of Agreements with Wells Fargo Bank

City staff is in the process of finalizing the negotiations with Wells Fargo Bank on four separate agreements for service. These agreements include the Master Agreement for Treasury Management Services ("General Banking Services" or "Master Agreement"), Merchant Card Processing Services, Lockbox Services and Securities Custody Services. There are several terms and conditions that are consistent throughout the four agreements in addition to terms and conditions that are specific to the service being provided.

Common Terms and Conditions:

- **Term of the Agreement(s)** – The term of the agreements for General Banking Services, Merchant Card Processing Services, and Lockbox Services commences upon execution of the agreements by the parties (anticipated to be on or about May 15, 2009) and continues through June 30, 2012 (the “Initial Term”), with the exception of the Security Custody Agreement that commences July 1, 2009. The City Manager and the City Manager’s authorized designees (collectively, “City Manager”), and the Director of Finance and the Deputy Director of Finance – Treasury, each, individually, has the option to extend the Initial Term of one or more of the Agreements in two-year increments (each, an “Option Period”) up to a maximum of six (6) additional years, through June 30, 2018. The City exercises this option by providing the Bank with written notice at least thirty (30) days prior to the expiration of the Initial Term or the Option Period, whichever is applicable.
- **Funding of the Agreement(s)** – The City’s funding of the Agreements is on a fiscal year basis (July 1 to June 30) and is subject to the annual appropriation of funds. The Bank and City both agree that the Initial Term of the Agreements and the exercise of any Option Periods are contingent upon the appropriation of funds by the City. The Agreements terminate immediately if funds necessary to continue the Agreements are not appropriated.
- **Compensation** – Total maximum annual compensation under all four agreements is \$864,000 per year, with each agreement having a maximum annual compensation based on estimated volumes of services. The maximum annual compensation may vary each year depending on the volumes of the various banking services; however, the schedule of fees is set for the Initial Term. The total compensation for the first year represents over 20% annual savings in the banking services costs, or nearly \$236,000 per year. All four agreements will be subject to a single total appropriation. In order to best manage the City’s overall banking costs, the Director of Finance and the Deputy Director of Finance, each, individually, is authorized to reallocate monies due under the agreements provided that the total maximum annual compensation for all four agreements does not exceed the amount annually appropriated.

For example, over time the City may experience more payments by credit cards than by check, thereby increasing compensation due under the Merchant Card Service Agreement and decreasing compensation due under the General Banking Services Agreement. The flexibility will allow the City to more efficiently manage all four agreements with Wells Fargo Bank and respond to changes in the use and demand for banking services. To that end, the Director of Finance and the Deputy Director of Finance, each, individually, is authorized to enter into amendments to the agreements without further Council approval; increasing or decreasing the Maximum Annual Compensation for each agreement provided such funds have been annually appropriated and the total maximum annual compensation does not exceed the appropriated funds.

Table 7
WELLS FARGO - BANKING SERVICES
ESTIMATED FIRST YEAR ANNUALIZED COSTS

	<u>Annualized Costs</u>
General Banking	\$228,000
Merchant Card	547,000
Lockbox	71,000
Securities/Custody	<u>18,000</u>
Total Annualized Costs	\$864,000

- **Indemnity and Limitation of Liability** -- Extensive negotiations between City staff and Wells Fargo Bank representatives have occurred concerning the indemnity and limitations of liability provisions in each of the proposed agreements. During these negotiations, Wells Fargo expressed its desire to limit its exposure to the City for consequential damages and its obligation to indemnify and hold the City harmless from liability that the City may incur as a result of Wells Fargo's performance under the agreements.

As an overview for the discussion of the specific provisions provided in the balance of the report, consequential damages, otherwise known as special or indirect damages, are one kind of two types of damages (the other being direct damages) that may be awarded to a plaintiff in a civil action who claims that terms of an agreement were not honored. As an example, in the case of a breach of a contract related to faulty construction of a building, direct damages would be the owner's costs of correcting the building defects. Consequential damages include loss of product and loss of profit or revenues and may be recovered if it is determined such damages were reasonably foreseeable at the time of the making of the contract. This is a factual determination that could lead to the contractor's liability for loss of operating revenue an owner might claim as a result of not being able to use the building as intended.

A number of the provisions described in the specific sections of the memo describing agreements and/or services shift the risk of loss to the City as opposed to Wells Fargo. Staff reviewed the proposals of the other banks that responded to the RFP and determined that the other respondents initially proposed provisions similar to those initially proposed by Wells Fargo. As these types of provisions appear to be common in the banking industry and in view of the revisions that Wells Fargo has agreed to, staff recommends that the City proceed with finalizing the agreements including the provisions described in the following Indemnity and Limitation of Liability sections.

General Banking Services:

Key Elements of the Master Agreement for Treasury Management Services ("Master

Agreement” or “General Banking Services Agreement”) include:

- **Services under the Agreement** – The terms and conditions of the Master Agreement control all other terms and conditions with respect to the City’s contractual relationship with Wells Fargo Bank unless defined elsewhere. This Agreement includes: services for contract for deposit of moneys, acceptance, service descriptions for each general banking service (“Service”), account agreement for commercial deposit accounts, user guides (including software, software licenses, reset diskettes, price schedules, specifications, instructions, and notices); and the set-up form(s) for each Service. The specific Services under the Master Agreement are described in detail below.
- **Changes to Services** – The Bank may change (or add to) the terms and fees of a particular Service at any time upon thirty (30) days prior written notification to the City and with the City’s written consent. The City may discontinue an existing Service or begin using a new Service by providing the Bank with at least thirty (30) days written notice. For new Services, the City’s Director of Finance and Deputy Director of Finance – Treasury are each, individually, authorized to enter into supplemental agreements for such Services, provided that:
 - (1) The cost of such new Service does not cause the compensation payable to Bank to exceed the maximum compensation permitted under this Master Agreement.
 - (2) The terms and conditions of this Master Agreement govern all supplemental agreements for new Services.
- **Termination** – The City has the right to terminate the Master Agreement, without cause, by giving not less than 90 days written notice to the Bank. The Bank may terminate the Agreement without cause, by giving not less than 180 days prior written notice to the City. The City may terminate the Agreement immediately if the Bank fails to perform its material obligations under the Agreement.
- **Compensation** – Total maximum annual compensation under the Master Agreement is \$228,000 per year. During each Option Period, the Maximum Annual Compensation may be increased by an amount no greater than the percentage increase in the Consumer Price Index for the calendar year (January through December) immediately preceding the first year of each Option Period multiplied by the Maximum Annual Compensation, or 3%, whichever is less.
- **Indemnity and Limitation of Liability** -- The Master Agreement for Banking Services and the Security Custody Services Agreement contain identical indemnity provisions. Wells Fargo and the City each agree to indemnify, defend, and hold harmless the other from all claims and losses (including attorney’s fees and costs) arising out of the performance of the services in the agreements caused in whole or in part by the negligent or intentional acts or omissions of their officers, directors, employees, agents or assigns. This provision generally requires that principles of comparative fault will be followed

and each party shall bear the proportionate cost of any damage attributable to the fault of that party, or its officers, directors, employees or assigns.

The Master Agreement for Banking Services Agreement also provides that neither the City nor Wells Fargo will be liable for special, consequential, or indirect damages, except in instances where the parties have acted with gross negligence or engaged in willful misconduct. Negligence is failure to act with reasonable care. Gross negligence means acting with serious carelessness, or acting in a way that is an extreme departure from the ordinary standard of conduct.

Both parties are liable for direct monetary damages for acting negligently or breaching the terms and conditions of the Banking Services Agreement. Initially, Wells Fargo capped the amount of direct damages it would be liable for to the City in connection with the Banking Services Agreement. However, after lengthy negotiations with Wells Fargo on this point and many others, Wells Fargo eventually agreed to eliminate its cap on direct monetary damages. However, the parties have agreed that neither party may be held liable to the other for punitive damages (which are awarded in certain instances to punish the offending party and go above and beyond what is required to make an injured party whole), in order to address Wells Fargo's concern over liability exposure to the City.

Unless otherwise set forth in the memo, each of the service descriptions described below will have the same, or similar, indemnity and limitation of liability provisions as contained within the general banking services provided by Wells Fargo, as set forth in the Master Agreement described above.

- **Specific Service Agreements** -- As part of the overall General Banking Services Agreement with Wells Fargo Bank, it is necessary to enter into a number of service agreements, which provide the City with the ability to either immediately commence utilization of the variety of specialized services offered by the Bank or to exercise an option to use these services in the future. These additional service agreements are briefly described below and it is anticipated that the utilization of many of these services will enhance customer service, increase operational efficiency and reduce the processing of large volumes of paper traditionally experienced in a banking relationship. During the Initial Term and any Option Periods, additional service agreements may be entered into by the Director of Finance or Deputy Director of Finance – Treasury without City Council approval, provided that there is no increase in overall compensation to the Bank.
 - **Account Reconciliation Plan (“ARP”) Service** – Allows for the Bank to receive a file of check issuance from the City. This data is then compared to the paid check detail with the end result being a fully reconciled account statement. The City will be able to receive back from the bank reports via the Bank's online portal with the outstanding checks detail and exception items.
 - **ACH Origination Service** – Allows for the City to originate automated clearing house (“ACH”) credit and debt entries in accordance with the National

Automated Clearing House Association Operating Rules and any applicable local ACH rules (collectively, the "ACH Rules"). The use of this service eliminates paper check processing through the Bank. Examples of ACH services include direct deposit of payroll, direct payment of customer bills, and business-to-business payments.

- **Indemnity and Limitation of Liability** -- For ACH Origination Services where the Bank is relying on instructions from the City and acts as a conduit of information between the City and a third party. The City is obligated to indemnify and hold harmless Wells Fargo for losses arising out of the City's own acts and omissions and for Wells Fargo's own negligence when relying on the City's instructions, but not for losses and liabilities arising from Wells Fargo's gross negligence or willful misconduct.

- **CEO Service** – CEO Services is the Wells Fargo internet portal that allows the City to access and/or download a multitude of financial applications and banking information related to the City's account(s). The site allows for anywhere, anytime access to the City's banking services, which is a key functionality in the event of a disaster. In addition to the maintenance of "state of the art" security, the City will have self-administration capabilities (with dual controls) for access and will be able to monitor use and access throughout the organization.

- **Commercial Account Agreement** – Defines the responsibilities and obligations of the City and the Bank with respect to the City's commercial bank account with Wells Fargo. Specific services and obligations of both parties under the Agreement include: applicable terms to commercial accounts, statements and other account related information, fraud prevention, claim of unauthorized transactions and Bank's rights and liability, substitute checks ("Check 21"), deposits to City's account, withdrawals from City's account, stop payment orders and notices of post-dating, overdrafts, Security Interest, Bank's Right to Set-off, Bank Fees and Expenses, checking subaccounts; interest-bearing accounts, funds transfers and selected services including ATM deposit and Treasury Express Deposit® Service.

- **Controlled Disbursement Service** – A service that provides same day notification of the dollar amount of the checks that will clear against the account designated as the controlled disbursement account, which allows for the City to control the flow of checks through the banking system and provides for more efficient cash management.
 - **Indemnity and Limitation of Liability** – In situations where Wells Fargo is relying on information provided by the City, the City is obligated to indemnify and hold harmless Wells Fargo and each disbursing bank from losses arising out of the City's own acts and omissions (for example, the City's failure to deposit collected funds).

- **Desktop DepositSM – CEO® Service** – Allows the City to use hardware provided by the Bank in conjunction with the Bank’s Commercial Electronic Office (“CEO”) portal to create electronic images of certain paper items and to transmit an electronic file of these images and other information to the Bank for deposit into the City’s account.
 - **Indemnity and Limitation of Liability** -- For Desktop Deposit (CEO Services) where the Bank is relying on instructions from the City and acts as a conduit of information between the City and a third party, the City is obligated to indemnify and hold harmless Wells Fargo for losses arising out of City’s own acts and omissions and for Wells’ Fargo’s own negligence when relying on the City’s instructions, but not for losses and liabilities arising from Wells Fargo’s gross negligence or willful misconduct.

In connection with the Desktop Deposit (CEO Services), the City is also obligated to indemnify and hold harmless Wells Fargo for the City’s material breach of a representation, warranty, covenant, or obligation contained in the service description, and the City’s violation of any applicable law, statute, or regulation in the performance of its obligations under the service description.

- **Escrow Account Services** – Periodically, the City needs to establish an escrow account for funds or documents related to various financial and/or real estate transactions. Wells Fargo will provide this service upon request for a set fee that eliminates the future need for the City to issue an RFP for this limited service, expedites the escrow establishment process, and simplifies with the services being provided by the City’s commercial bank.
- **Information Reporting Service** – Allows the City, through the use of a computer and/or a computer and browser acceptable to the Bank, to receive account balance and other types of account information related to the City’s deposit account.
- **Positive Pay – Return Default Service** – This service is a check fraud reduction program that enables the City to instruct the Bank to return counterfeit checks or checks not validly issued, including certain altered checks presented to the bank for payment.
 - **Indemnity and Limitation of Liability** -- For Positive Pay Return Default Services, the City agrees to indemnify and hold harmless Wells Fargo from any losses Wells Fargo may suffer as a result of Wells Fargo's payment of a matching check, or other check, at the City's instruction and releases Wells Fargo from any claim the City might have against Wells Fargo relating to Wells Fargo's payment or return of any check; provided Wells Fargo adheres to its obligations under this service.
- **Receivables Manager Service** –Allows for the City to send and receive remittance information and related data through various communication channels

including paper. The City can elect to have the Bank consolidate all remittance information into a single transmission to enable the City to appropriately update its various account receivable systems.

- **No Liability of Third Party Service Provider or Customer Financial Institution** -- Under the Receivables Manager Service, Wells Fargo registers the City as eligible to receive electronic bill payments. A customer of the City can then make payments to the City by using its own bank's (Customer Financial Institution) online banking service. Such Customer Financial Institution will in turn debit the funds from its customer's account and send the funds to the City's Wells Fargo account by using a third party service provider, such as MasterCard International. By virtue of the City using Receivables Manager, the third party service provider (which is acting as a mere clearing house for bill payments) and the Customer Financial Institution (which is sending funds to the City's Wells Fargo account as instructed to by its customer) are not liable to the City for any damages arising out of the City's use of this service. The City's recourse would be against the Bank or its own customer, as the case may be.

- **STOPS—IMAGES—SEARCH (“SIS”) Service** – Allows the City to request a stop payment order on a check drawn on the City’s deposit account and to request photocopies of checks that have cleared the City’s deposit account and/or controlled disbursement account.

- **Wells Fargo PayCard Service** – Allows for the City to make payroll payments and/or expense reimbursements to PayCard users who do not have designated traditional checking accounts for direct deposit. Employees or other payees can access deposits through certain national and regional ATM and Point of Sale (POS) networks, as well as any financial institution or merchant that accepts Visa debit cards. The Agreement with the Bank will allow for one free transaction at Wells Fargo ATMs per pay cycle.

- **Wells Fargo Stagecoach Sweep Service** – Allows for the City to link each demand deposit account to an investment option providing for interest earnings on amounts in the accounts. The City’s cash management function is designed to minimize the amount in the account. This service allows for any funds that would have been uninvested to be invested overnight in a designated “sweep account”. Authorized sweep account will meet the requirements of the Investment Policy.

- **WELLSIMAGE® CD Service** – Allows for the City to view Wells Fargo-issued CD-ROMs and Wells Fargo Image File Import posted items containing digital images of checks posted against the City’s accounts and the Lockbox Module, which allows the viewing of digital images of checks and associated images posted through the lockbox services. A license fee is paid for the use of the software.

- **License Agreement** -- Before the City can use the WELLSIMAGE CD Service described above, it must accept the terms and conditions of the WELLSIMAGE Viewer Software License Agreement (“License Agreement”). The License Agreement is an electronically presented form used by Wells Fargo that pops up on the end users screen and requires the end user to click “accept” in order to proceed forward with the service. If the end user clicks “decline,” then implementation of the program ends.

As part of the License Agreement, all end users, including the City, acknowledges that the software is owned by Wells Fargo and that they will not copy or reproduce the software except to the extent authorized by Wells Fargo. The end users agree to implement all necessary and reasonable procedures and controls to protect the confidentiality of the software and not to disclose the software to any person or entity except to employees requiring access to the software. Wells Fargo represents that to the best of its knowledge and its third party suppliers of the software, that the software is free from any generally known virus that would cause the software to function in a manner other than as provided in the specifications for the software or that would impair or damage any hardware of software system with which it might be used. However, neither Wells Fargo nor its third party suppliers of the software makes any representation or warranty to that effect or assumes any liability in such regard. The end users must therefore take such steps as are appropriate to protect their hardware and software systems and equipment from the existence of any virus or other device within the software. The software is provided “as is” without warranty of any kind either express or implied. The entire risk as to the quality and performance of the software is with the end users (and in this instance, the City). Neither Wells Fargo nor its third party supplier of the software will have any liability to the City for any losses including, but not limited to, lost data or damages for monetary business loss incurred by the City as a result of, or in any way connected with, the software, regardless of whether the losses are in any way connected with Wells Fargo’s misrepresentation or breach of an express or implied warranty, or negligence, breach of contract, strict liability, or otherwise. Further, in no event will the total aggregate liability (under any theory of liability) of Wells Fargo or any third party supplier of the software arising out of, or in any way connected with the use of the software, exceed the license fee paid by the City for the software

- **Wire Transfer Services Security Procedures Agreement** – Provides the terms, conditions and responsibilities of the City with respect to wiring funds from the City’s accounts with the Bank. Agreement also provides for self-administration by the City of the various accounts and access levels.

Merchant Card Processing Services

Merchant card services are provided for the servicing of credit card payments through the execution of the Merchant Agreement, which includes the Merchant Processing Application, the Program Guide and associated schedules and documents; which may be amended from time to time. The Agreement with Wells Fargo Bank will include servicing for Visa, MasterCard and Discover cards. This Agreement will include the terms and conditions for accepting, payment on and "charge-backs" for credit cards. The terms and conditions are primarily driven by the Association Rules for each Visa, MasterCard and Discover.

- **Services under the Agreement** – The services under the Agreement include the operating procedures for both the City and the Bank in the following areas: acceptance of Visa, MasterCard and Discover; procedures for suspect transactions; completion of sales and credit drafts; data security requirements; authorization procedures; submission and deposit of sales and credit card drafts; settlement; refunds/exchanges (credits); retention of records; chargebacks and other debits; account maintenance; and Association Rules compliance.

As part of the negotiations of the Merchant Agreement, there are several terms and conditions that warrant to be highlighted as future opportunities for the City and/or limitations with respect to the Agreement:

- **Convenience Fees** – The City will be allowed to impose a convenience fee within the terms, conditions and guidelines established by all of the Association (Visa, MasterCard and Discover) Rules. Staff will begin this examination process after the transition to Wells Fargo is complete and will return to Council with a recommendation.
- **Exclusive Merchant Card Vendor** -- The City will be required to use Wells Fargo Bank for all credit card processing services except for those relationships currently under contract (utility services, Parks & Recreation's pilot program with Active Network and Department of Transportation for parking fines). The more credit card payments that are consolidated under this agreement the more the City can benefit from the State pricing discussed below. In addition, it simplifies and consolidates the City's security requirements related to credit cards.
- **TeleCheck Services** – As part of the Merchant Card Processing Services Agreement, the City may enter into an agreement for TeleCheck Services with TeleCheck Services, Inc. ("TeleCheck") a third party provider. TeleCheck will be used at Point of Sale (POS) locations where checks presented and placed in a scanner for conversion to an ACH (electronic) payment. TeleCheck will provide the City with a confirmation code that warrants the check presenter has the funds in their account to cover the presented check. The City benefits from the funds from check presentment being available sooner than when a check is processed through normal channels. Additionally, the risk of accepting checks with non-sufficient funds is greatly reduced.

As part of the agreement with TeleCheck, in no event shall either TeleCheck or the City be liable to the other for any consequential or punitive damages. Further, TeleCheck's liability to the City for direct damages is capped at the total amount of fees paid to TeleCheck during the 12 month period immediately preceding the date of the event giving rise to the claim for damages, or \$75,000, whichever is less. The agreement is governed by and construed in accordance with the laws of the State of Texas. Finally, in the event the City breaches the agreement or terminates the agreement early without cause, then TeleCheck is entitled to recover from City liquidated damages in the amount equal to 90% of the aggregate monthly minimum fees and processing fees for the unexpired portion of the term of the agreement.

- **Termination** – The City has the right to terminate without cause by giving not less than 90 days prior written notice to the Bank. The Bank may terminate the agreement without cause, by giving not less than 90 days prior written notice to the City. If a party fails to perform its material obligations under this agreement, the non-breaching party may terminate the agreement immediately or provide the breaching party with an opportunity to cure before terminating the agreement.
- **Compensation** – Total maximum annual compensation under the Merchant Card Processing Services Agreement is \$547,000 per year. The City was able to secure fixed pricing for five (5) years from Wells Fargo Bank for their processing portion of the merchant card fees. The Wells Fargo fee is based on the pricing received by the State of California under their Master Service agreement with Wells Fargo, which expires in December 2009. A majority of the fees paid for merchant card services are derived from interchange rates/fees established by the credit card associations, which are subject to annual adjustments and are completely out of the City's ability to negotiate these fees. The total merchant card fees paid by the City is driven by the dollar volume of credit card charges, so to the extent dollar volumes increase the amount of the total fees paid by the City will also increase.
- **Indemnity and Limitation of Liability** -- For Merchant Card Services the City agrees to indemnify Wells Fargo and hold it harmless from losses and liabilities resulting from the City's breach of the agreement, the negligence or willful misconduct of its employees or agents in connection with card transactions, or any third party indemnification Wells Fargo is obligated to pay as a result of the City's actions. In turn, Wells Fargo agrees to indemnify the City and hold it harmless from losses and liabilities arising from its breach of the agreement or arising out of its employees' negligence or willful misconduct. Originally, Wells Fargo only agreed to indemnify the City if the City's losses resulted from Wells Fargo's gross negligence.

In addition, Wells Fargo's cumulative liability to the City for all losses, claims, suits, controversies, breaches or damages for any cause whatsoever and regardless of the form of action or legal theory, shall not exceed \$50,000 or the amount of fees received by the City pursuant to the Agreement for services performed in the immediately preceding 12

months, whichever is less. In no event shall either party be liable to the other for special, indirect, consequential, or punitive damages.

The Merchant Card Services Agreement also provides the City with the opportunity to purchase or lease equipment from Wells Fargo or one of its third party vendors. Each of the purchase and lease agreements within the Merchant Card Services Agreement contains similar provisions whereby the City is obligated to indemnify and hold harmless the provider of the equipment for damages arising from the City's own acts and omissions and breach of the purchase or lease agreement except to the extent damages result from the providers own gross negligence or willful misconduct. The provider's liability for direct damages to the City is capped at the amount of rent received by the provider for the leased equipment or the purchase price of the equipment, as applicable. The provider is not liable for indirect, special, or consequential damages.

- **Liquidated Damages for Early Termination** – If the City terminates the agreement without cause prior to the end of the Initial Term (June 30, 2012), the City shall pay an early termination fee to be calculated as follows: termination in the first year of the Initial Term fee is equivalent to 0.06% of the annual Net Credit Card and Non-PIN DEBIT (MasterCard/Visa/Discover Network) volume ("Sales Volume"), which was estimated by the City on the Merchant Processing Application; if the City terminates during the second year of the Initial Term the fee is equal to 0.04% of the merchant's total sales volume for the preceding 12 months; and if the City terminates during the third year of the Initial Term, the City shall pay an early termination fee of 0.03% of the merchant's total sales volume for the preceding 12 months. These early termination fees could range from (\$16,200 in the first year to approximately \$8,000 in the third year).

Lockbox Service

Lockbox services are offered by commercial banks as a way to simplify and expedite the collection and processing of account receivables by having payments mailed directly to a location, generally a post office box that is accessible by the bank. The bank is then responsible for processing the payments to the City's bank account.

Key elements of the Lockbox Services Agreement include:

- **Services under the Agreement** – Directions with respect to the disposition of remittance materials including: check depositing parameters and documents included with remittance, daily deposit of checks and cash including endorsement of checks.
- **Termination** – The City has the right to terminate with not less than 90 days notice to the Bank. The Bank may terminate the agreement without cause, by giving not less than 180 days prior written notice. The City may terminate Agreement for failure to perform material obligations under the Agreement.
- **Compensation** -- Total maximum annual compensation under the Lockbox Services Agreement is \$71,000 per year. During each Option Period, the Maximum Annual

Compensation may be increased by an amount no greater than the percentage increase in the Consumer Price Index for the calendar year (January through December) immediately preceding the first year of each Option Period multiplied by the Maximum Annual Compensation, or 3%, whichever is less.

- **Limitation of Liability** -- For Lockbox Services where the Bank is processing payments sent into the Lockbox by a third party at the City's request at a nominal fee for each item processed, Wells Fargo's liability is limited to the amount of interest the City would have otherwise earned if the checks had been properly processed and deposited, and for any other action or failure to act in violation of the agreement. Money damages are limited to three (3) times the service fees charged during the month immediately preceding the month in which the loss occurred, or \$200,000, whichever is less.

Securities Custody Services:

Custodial services are a common element generally included as part of the banking services. In today's electronic world, most securities do not exist in physical form, but are rather "electronically" held in book entry form on behalf of the owner. The most efficient way to meet the required delivery of securities is through a third-party custodian, which is usually a bank. The days of physically holding securities in paper form in a vault with the owner (local agency) are long gone. The use of third-party custodians ensure that no funds are at risk in the transaction since funds are not released to pay off the securities until they are delivered. The delivery versus payment aspect of these transactions means that the local agency should be holding either money or securities at all times during the transaction.

Key elements of the Securities Custody Agreement include:

- **Services Under the Agreement** – Settlement of investment transactions; collect the interest and principal paid on the securities held on behalf of the City; issue advices setting forth the specifics of purchases, sales, receipts, deliveries and principal collection; deliver cash or securities as directed by an authorized City representative; provide notification of call notices of securities held in the Account; and provide a monthly statement setting forth inventory of assets in the Account and market value of each asset, which may be provided either in printed or electronic format. The Agreement only covers the City's Investment Portfolio and does not provide services for the Employees Deferred Compensation Plan, the Federated City Employees Retirement System or the Police and Fire Retirement Plan, which are covered under separate agreements.
- **Termination** – The City has the right to terminate the Securities Custody Services Agreement, without cause, by giving not less than 90 days prior written notice to the Bank. The Bank may terminate the Agreement without cause, by giving not less than 180 days prior written notice to the City. The City may terminate the Agreement immediately if Wells Fargo fails to perform its material obligations under the Agreement.
- **Compensation** – Total maximum annual compensation under the Securities Custody Agreement is \$18,000 per year. During each Option Period, the Maximum Annual

Compensation may be increased by an amount no greater than the percentage increase in the Consumer Price Index for the calendar year (January through December) immediately preceding the first year of each Option Period multiplied by the Maximum Annual Compensation, or 3%, whichever is less.

- **Indemnity and Limitation of Liability** -- The Security Custody Services Agreement contains identical indemnity provisions as the Master Agreement for Banking Services.

EVALUATION AND FOLLOW-UP

This memorandum presents the set of recommendations related to the City Council's approval of four agreements with Wells Fargo Bank, N.A. to provide services related to the City's general banking, merchant card services, lockbox services and security custody services. In addition, a recommendation to enter into a one-year agreement with Union Bank of California to provide limited banking services related to the processing and payment of checks issued by the City that are still outstanding. Staff will research the ability to implement a credit card convenience fee after the banking services transition is complete and will report back on the findings to the City Council.

PUBLIC OUTREACH/INTEREST

This memorandum will be posted on the City's website for the May 5, 2009, agenda. This memo was included in the Early Distribution Council packet.

- Criteria 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- Criteria 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- Criteria 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

COORDINATION

This staff report has been prepared by the Finance Department in coordination with the City Attorney's Office, the Information Technology Department, and the City's Manager's Budget Office.

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FISCAL/POLICY ALIGNMENT

This item is consistent with General Budget Guidelines in that the agreement with Wells Fargo Bank has a positive effect on the fiscal integrity and flexibility of the City and it is consistent with the following City's Budget Balancing Strategy Guidelines; "focus on protecting vital core City services" and "focus on improving employee productivity and business practices".

COST SUMMARY/IMPLICATIONS

The City currently appropriates \$1,050,000 for general banking services and \$50,000 per year for securities custody services for a total budget appropriation of \$1,100,000. These funds cover the ongoing costs of the new agreement with Wells Fargo Bank, one-time costs associated with the transition of the banking services, which includes staff time, technology enhancements and equipment purchases, and the one-year agreement with Union Bank of California to cover the services associated with maintaining an account to process payment of checks issued, but not yet presented at the time of the conversion from UBOC to Wells Fargo.

BUDGET REFERENCE

The table below identifies the funds and appropriations proposed to fund the actions recommended in this memorandum.

Fund	Appn.	Appn. Name	Total Appn.	2008-09 Adopted Budget Page	Last Budget Action (Date, Ord. No.)
001	2987	Banking Services	\$1,050,000	IX-18	6/24/08, Ord. No. 28349
001	2974	Securities Custody Services	50,000	IX-20	6/24/08, Ord. No. 28349

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CEQA

Not a project.


JULIA H. COOPER
Deputy Director, Finance

For questions, please contact Julia H. Cooper, Deputy Director of Finance, at (408) 535-7011.