



City of Palo Alto

City Council Staff Report

(ID # 11402)

Report Type: Consent Calendar

Meeting Date: 9/21/2020

Summary Title: Banking and Related Service Contracts Amendments for Extension

Title: Approve Contract Amendments to Extend the Following Banking and Related Services Contracts: 1) U.S. Bank and its Wholly-owned Subsidiary Elavon for General Banking and Merchant Services; 2) Wells Fargo for Lockbox Services; 3) Union Bank for Investment Safekeeping (Custodial) Services; and 4) JP Morgan Chase Bank for Purchase Card (P-card) Services

From: City Manager

Lead Department: Administrative Services

Recommendation

Staff recommends that the City Council approve four contract extensions for banking and related services, extending the contract terms as noted below, effective July 1, 2020:

- 1) U.S. Bank and its wholly owned subsidiary, Elavon, for general banking and merchant services ([Attachment A](#)), extending the term for three years, beginning July 1, 2020;
- 2) Wells Fargo for lockbox services ([Attachment B](#)), extending the term for three years, beginning July 1, 2020;
- 3) Union Bank for investment safekeeping (custodial) services ([Attachment C](#)), extending the term for two years, beginning July 1, 2020; and
- 4) JP Morgan Chase Bank's cloud-based and paperless purchase card services (P-Card) ([Attachment D](#)), authorizing the continuation of the contract between the City and JP Morgan Chase executed on July 1, 2014.

Executive Summary

This report recommends the approval of an up to two- or three-year extension for banking services contracts and related services, extending the contracts to a total term of eight or nine years. These four contracts were originally approved by the City Council in FY 2014 after a Request for Proposal (RFP) process for the purpose of increasing competition among banking

service and related providers and lowering costs. Services provided by these four contracts include: (1) general banking and merchant (credit and debit card acceptance), (2) lockbox (processing of utility bill check payment), (3) safekeeping or custodial (settlement, safekeeping, and reporting of investment security), and (4) purchase (credit) card (P-Card) services. Under these contracts, pricing achieved and awarded in FY 2014 will continue through the extended term without any annual increase to unit prices. The current vendors have agreed to keep or lower the current prices for the next three years except for Union Bank, which has only committed to a two-year extension at current prices. Therefore, the City will continue to receive FY 2014 fixed unit pricing through FY 2022 or FY 2023, eight to nine years.

Due to the imbedded nature of banking contracts in day to day financial transactions of City business, it is not uncommon to see longer term contracts up to 10 years to ensure continuity of service and necessary strategic deployment of resources for major projects such as the implementation of a new banking relationship. Staff spent time reviewing the current services and analyzing comparatives to several other municipalities to ensure the pricing of these contracts remain competitive. Upon the completion of these recommended extended terms, staff expects to conduct a new RFP for these services.

These contracts are structured based on service and activity level; the City essentially controls costs via a fixed payment per service during the length of the contracts. Therefore, staff recommends continuation of the previous contract terms that do not include a “not-to-exceed limit”, as cost is dictated by transaction volume which can change over time. Staff has and will continue to closely monitor costs on a regular basis. In total, net annual costs for these contracts have remained at or below \$100,000 annually while rebate revenue from the P-Card service has been above \$135,000.

Below is a summary of the recommended agreements:

- 1) U.S. Bank and its wholly owned subsidiary, Elavon, for general banking and merchant services (a three-party agreement). U.S. Bank and Elavon have agreed to continue the same transaction prices for the next three years that were agreed to in the original contract in FY 2014. Average annual spending of \$20,000: a net \$14,200 (gross expense of \$50,200 offset by rebates of \$36,000) for general banking and \$9,500 for merchant services (bank fee only). ([Attachment A](#))
- 2) Wells Fargo (Wells), provides lockbox services. This extension reflects a reduction in the current lockbox transaction cost by 10 percent; an average annual savings of \$3,100. Average annual expenses of \$30,800. ([Attachment B](#))
- 3) Union Bank (Union) provides investment safekeeping (custodial) services. This two-year extension continues the same transaction prices that were agreed to in the original contract in FY 2014. Average annual expenses of \$29,000. ([Attachment C](#))

- 4) JP Morgan Chase Bank's (JP Morgan) provides cloud-based and paperless purchase card services (P-Card). This is a revenue (rebate) contract where there are no service fees. Average annual rebate revenues of \$148,500, which has increased 16.3 percent the prior three years due to higher activity level by the City. The current rebate rate remains unchanged in this extension term. ([Attachment D](#))

The proposed contract extension term for each provider is two or three years, starting July 1, 2020 to June 30, 2022 or 2023. The contract with JP Morgan Chase does not contain a term end, and staff is requesting that Council authorize the continuation of the City's banking contract with JP Morgan for the City's P-Card program. For the four contracts, during the last three years, (per Table 1) the City's total (cumulative) rebates or revenues was \$445,500 while costs were \$214,000 resulting in net earnings of \$231,500. The three-year net annual average net earnings were \$74,000. Similar results are forecasted for the next two or three years should the recommended contract extensions be approved. In each contract, the City and the banking services provider each retains the option to terminate the contract upon 30-day notice.

Background

In 2005, the City conducted an RFP process for banking related services. After reviewing the proposals from several banks, the City selected Wells Fargo (Wells) for general banking services. The selection of Wells ended a long-term relationship with Bank of America, the prior banking services provider. The agreement with Wells consisted of a three-year contract plus an additional two-year extension. That five-year service contract and extension ended on December 31, 2010.

In November 2010, staff requested that Council extend the existing contract with Wells for three years, rather than initiate a new RFP. This approach was taken at the depth of the recession for a number of operational and cost related issues. Lower fees were successfully negotiated with Wells during this time and the extension was approved by Council.

As a result of a more complex evaluation process, staff requested and City Council approved on December 9, 2013 ([ID # 4284](#)), a one-year banking services contract extension from January 1, 2014 to December 31, 2014. Staff did not request separate contract extensions for lockbox and merchant services because their contract dates had not expired.

The Purchase Card (P-Card) did not expire until January 2015 but to evaluate options and pricing, these services were included in the RFP performed in 2014. Of the firms responded, JP Morgan (the City's current P-Card provider) offered the highest rebate rate of all the proposers.

In June 2014, based on the RFP results and staff recommendation, Council awarded contracts ([ID # 4905](#)) to the following financial institutions:

- 1) U.S. Bank and Elavon for banking and merchant services,
- 2) Wells Fargo for lockbox service,

- 3) Commerce Bank for a new and innovative Accounts Payable bill payment service,
- 4) Union Bank for investment safekeeping (custodial) service, and
- 5) JP Morgan Chase Banks for purchase card (P-Card) service.

The contracts were for six years from July 1, 2014 to June 30, 2020. The Commerce Bank's Accounts Payable bill payment implementation was halted and then discontinued as the service was unable to meet the City's needs as was originally expected as part of their proposal.

Discussion

After an evaluation of the offered bank fees and comparison to other agencies, staff recommends that Council extend the agreements with the City's current banking and P-Card service providers. In addition to competitive pricing, customer service level and user-friendly on-line portals, the current service providers are willing to extend or reduce the current pricing for the next two or three years. Wells Fargo proposes a 10 percent cost reduction, while all other banks held pricing and/or rebates. Though staff asked all service providers for pricing concessions, U.S. Bank, Elavon and Union Bank stated Palo Alto has their lowest prices which is supported by staff's experience based on the last RFP and by comparisons to other municipalities. Due to the above and increased complexity of the financial services used by the City, having the flexibility to address the current financial constraints, and the evaluation process being more complicated and more time-consuming, extending these contracts are prudent to balance available staff resources while still obtaining competitive service, costs, and/or rebates. Per Table 1 (see Timeline and Resource Impact section), the four contracts net total activities earn revenue for the City of several hundred thousand dollars.

1) Banking and Merchant (credit and debit card) Services:

Banking services include, for example: maintaining the City's various checking accounts, wiring funds for purchases of goods and overnight deposits, processing cash, processing payroll and bill payments, providing a variety of reports to enhance cash management, downloading files to update City financial system, and merchant services. For these services, U.S. Bank and Elavon provides a range of products including a dedicated team for customer support. Also, they provide a user-friendly Internet portal that staff can use to perform banking services tasks including monitoring and preventing fraudulent activities, wiring funds, and obtaining reports.

Typically, the main difference between similar service providers is cost. In the RFP performed in 2014 U.S. Bank was the lowest bidder and provided a proposal that was 43.2 percent lower than the banking fees at that time and 32.7 percent lower than the second lowest bidder. In addition, Elavon's pricing proposal, for merchant service, was not priced as a percentage of credit card charges (typically 0.05 percent to 0.075 percent of the charged amount). Instead, Elavon quoted a fixed fee per transaction of 10 cents. As a result, its cost then was 53.6 percent lower than the second lowest proposal. Most of the credit card processing cost is attributable to the card networks. For both, the U.S. Bank and Elavon have proposed to continue these low prices for the next three years.

It is important to note that the majority of the credit card fees are attributable to the credit card (brand) networks (e.g., VISA, MasterCard, etc.). These network fees are not negotiable, so they were not included in the contract pricing. Only bank fees, which are for the portal to the card networks, were evaluated in the RFP.

U.S. Bank merchant services are provided through Elavon, a wholly owned subsidiary of U.S. Bank. The Elavon's merchant services annual average costs were around \$9,500 the past three years. Elavon is one of the largest (credit and debit) card processor in the United States; with more than 1.2 million merchants using its services. In FY 2019, the City's total credit card expense, including Elavon's fee, was \$1.3 million.

The annual net general banking services cost (gross banking fees less earning credit and rebates) for the last three years ranged from \$13,200 to \$17,500. The current Palo Alto U.S. Bank fees compared to City of Mountain View and City of Santa Clara is 77.3 percent lower and U.S. Bank's recent fee proposal to the City of Livermore is 27 percent higher than Palo Alto current costs. This supports U.S. Bank's assertion that Palo Alto is receiving their lowest pricing.

For the Dakota Pipeline Project (DAPL), per Wells Fargo, they were one of 17 banks with commitments to the \$2.5 billion DAPL credit facility. Wells Fargo's loan represented less than 5 percent of the total financing for the project. Wells Fargo represented the DAPL project was evaluated by an independent engineer to be compliant with the [Equator Principles](#), a framework adopted by Wells Fargo in 2005 that is designed to determine, assess, and manage social and environmental risks and impacts of projects. The DAPL term loan was refinanced in the private placement market in March 2019, ahead of its August maturity, and Wells Fargo no longer has a direct lending relationship to DAPL.

Staff is recommending that the banking and merchant services contract with U.S. Bank and Elavon be extended for the next three years with the same terms which will provide the services the City requires and continuing the current pricing structure.

2) Lockbox Services:

This services contract outsources the processing of utility check payments. As with banking and merchant services, lockbox services are provided by many financial institutions, including the U.S. Bank. However, Wells was selected in the last RFP since they were the lowest bidder. The cost, based on the past three-year activity level, ranges from \$25,500 to \$35,500 annually (net cost after earning credit ranges for the same period from \$20,300 to \$23,700). Wells has proposed to reduce the current contract cost by 10 percent. A comparison to City of Mountain View and City of Livermore shows the current contract prices, before the proposed 10 percent cost reduction, to be lower by 39.4 percent and 30.1 percent respectively.

Staff recommends the lockbox services contract be extended for three years with Wells Fargo Bank.

3) Investment Safekeeping (Custodial) Services:

Safekeeping or custodial services include taking custody of investment securities purchased by the City; paying interest and principal due from securities; and providing monthly statements which show the book, par and market values of securities in the City's portfolio.

In the last two RFPs, performed in FY 2014 and FY 2005, Union Bank had the lowest cost. Annual actual cost the last three years ranged from \$27,300 to \$32,300. Service and online portals are similar among the banks. The City has been receiving excellent service from Union Bank for over three decades and it has been the lowest cost provider for that duration. A comparison to City of Santa Clara shows average quarterly cost to be 35.6 percent lower. Union Bank offered to extend the current pricing for only two years.

Renewal of the contract with Union Bank for two years, for custodial (safekeeping) services is recommended.

4) Purchase Card (aka P-Card) Services:

The purchasing card program is cloud-based payment solution that helps the City reduce costs and simplifies the procure-to-pay process. It solidifies purchasing controls while allowing the flexibility to purchase goods and general services, the City to leverage transaction data for more informed decisions and better vendor management, paperless transaction processing and statement review, and a more complete picture of spending patterns. As a result, employees are spending less time authorizing, tracking and processing expense transactions.

Over the years P-Card charges went from \$0.2 million in FY 2005 to \$8.7 million in FY 2019 and the current fiscal year (2020) is forecasted to decline to \$7.5 million. At the same time, A/P check issuances went from a high of 25,600 to estimated 8,200 for the FY 2020 resulting in improved efficiency and savings. Approximately 321 City purchasing cards are in use generating \$158,400 in revenue during calendar year 2019 calculated based on the following consortium table at a rate of 1.68 percent.

During the last RFP, of all firms responding, JP Morgan (the then existing service provider) had the highest rebate which has increased 16.3 percent over the last three years and having a robust system that allows directly attaching store receipts to a transaction on JP Morgan’s on-line portal. The latter streamlines the internal approval process and record retention. This makes the current paperless system possible. The higher rebate is attributable to the City joining JP Morgan’s payment solution consortium, an option that become available to California municipalities, originated by the City of Fort Worth (Texas). The consortium’s revenue (rebate) rate takes into consideration the total consortium and individual member charges volume as shown in the following table.

Annual Consortium Combined Total Charge Volume	Combined Total Charge Volume of Individual Participant				
	\$500,000 to \$999,999	\$1,000,000 to \$7,999,999	\$8,000,000 to \$19,999,999	\$20,000,000 to \$39,999,999	\$40,000,000 or more
	Volume Rebate Rate @ 29-day Average File Turn	Volume Rebate Rate @ 29-day Average File Turn	Volume Rebate Rate @ 29-day Average File Turn	Volume Rebate Rate @ 29-day Average File Turn	Volume Rebate Rate @ 29-day Average File Turn
\$25,000,000	0.80%	1.50%	1.53%	1.56%	n/a
\$75,000,000	0.85%	1.55%	1.58%	1.61%	1.64%
\$150,000,000	0.90%	1.57%	1.60%	1.63%	1.66%
\$200,000,000	0.95%	1.59%	1.62%	1.65%	1.68%
\$300,000,000	1.00%	1.60%	1.63%	1.66%	1.69%
\$400,000,000	1.02%	1.60%	1.64%	1.68%	1.72%
\$500,000,000	1.02%	1.61%	1.66%	1.70%	1.75%
\$600,000,000	1.02%	1.61%	1.68%	1.72%	1.77%
\$800,000,000	1.02%	1.62%	1.69%	1.73%	1.78%
\$1,000,000,000+	1.02%	1.62%	1.70%	1.74%	1.79%

For the above reasons, staff recommends JP Morgan Chase Bank P-Card contract be extended for three years.

Timeline and Resource Impact

These two or three-year contracts are from July 1, 2020 to June 30, 2022 or 2023 for; (1) banking and merchant services, (2) lockbox services, (3) investment safekeeping (custodial) services, and (4) purchase (credit) card (p-card) services. Staff is requesting a departure from the “not-to-exceed limit” on these contracts, as they are based on specific services, fixed prices, and City control over transactions. The contract has specific fixed durations and/or termination clauses. Finally, there are provisions for caps on future cost increases where appropriate. Caps do not apply to revenue-based contracts such as the purchase card agreement. Staff will closely monitor costs on a regular basis. All the current providers agreed to extend the current low prices except Well Fargo Bank which is lowering the cost by 10 percent.

Table 1

**Banking and Related Services
Historical Contracts Expenses and Revenues**

	3-Yr. Avg. Gross Actual Expenses (Annually)	3-Yr. Avg. Earnings / Rebates (Annually)	Net Avg. (Expenses) / Rebates (Annually)	Total Actual (Net Expenses) / Revenues for the Last 3-Yrs.
1) Banking Services Expense (U.S. Bank)	\$ (50,212)	\$ 35,939	\$ (14,273)	\$ (42,818)
2) Merchant (credit and debit card) Services Expense (Bank costs only; excludes credit card network fee) (Elavon)	(9,509)	-	(9,509)	(19,019)
3) Lockbox Service Expense (Wells Fargo)	(30,768)	9,008	(21,760)	(65,279)
4) Investment Safekeeping Service Expense (Union Bank)	(28,977)	-	(28,977)	(86,931)
5) Purchase Card (P-Card) Service <u>Revenue</u> (Rebate) (JP Morgan Chase Bank)	-	148,497	148,497	445,492
Net Actual (Expenses) / Revenues	\$ (119,466)	\$ 193,444	\$ 73,978	\$ 231,444

As stated, Table 1 expenses and rebates or revenues are based on the past three years of actual activity level and current contract (fee or revenue) rates with future actuals and corresponding expenses and revenues fluctuations depending on the activity level generated by the City. The merchant service cost cited above only represents the bank's portion of the fee. Majority of credit card fees charged to the City are attributed to the credit card networks (e.g. VISA, MasterCard). FY 2019 total credit card fees (citywide) were \$1.3 million; the budget for these expenses is included in the proposed FY 2021 budget.

- 1) U.S. Bank and its wholly owned subsidiary, Elavon, for general banking and merchant services. Actual past three years net average annual costs (gross banking fees less earning credit and rebates) for banking and bank portion of merchant fee (excludes VISA and MasterCard network or interchange fees) were \$14,300 and \$9,500, respectively. Over the last three years, total actual net costs, for general banking and bank merchant fees, were \$42,800 and \$19,000, respectively. U.S. Bank and Elavon have agreed to continue the same low transaction prices for the next three years that they agreed to six years ago, which effectively means U.S. Bank will be keeping the same transaction prices for a total of nine years. ([Attachment A](#))
- 2) Wells Fargo (Wells), for lockbox services, actual past three years net average annual costs were \$21,800 and over the past three years actual total costs were \$65,300. Wells has

agreed to reduce the lockbox transaction cost by 10 percent over the current contract prices; an average annual savings of \$3,100. ([Attachment B](#))

- 3) Union Bank (Union) for investment safekeeping (custodial) services. The actual past three-year average net annual costs were \$29,000 per year, with three-year total costs of \$86,900. Union has also agreed to continue the same low transaction prices for the next two years that as agreed to in 2014. ([Attachment C](#))
- 4) JP Morgan Chase Bank's (JP Morgan) cloud-based and paperless purchase card services (aka P-Card). This is a revenue (rebate) contract where there are no service fees. In the prior three years, rebate revenue has increased 16.3 percent due to higher activity level by the City and higher rebate rate offered by JP Morgan. ([Attachment D](#))

The preceding Table 1 summarizes the last three years of actual contracts expenses and revenues. For the four contracts, the City earned a net rebate or revenue of \$231,400 and the net average annual revenue was \$74,000. Similar results are forecasted for the next two or three years should the recommended contract extensions be approved.

The proposed contract extension term for each provider is two or three years, starting July 1, 2020 to June 30, 2022 or 2023, with the exception of the agreement with JP Morgan that does not contain a contract end term. In each contract, the City and the banking services provider each retains the option to terminate the contract upon 30-day notice.

Stakeholder Engagement

For the duration of these contracts, Administrative Services staff have coordinated with City staff to resolve any issues. Most of these have been routine reconciliation, confirming a validity of a transaction, and/or information inquiries to clarify an activity so, as a whole, it's known the organizations satisfaction with these services has been high. The expectation is this will continue with the proposed contract extensions.

Environmental Review

The award of a banking services agreement is not considered a project under the California Environmental Quality Act; therefore, an environmental review is not required.