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ERIC GARCETTI
MAYOR

November 21, 2017

Honorable Members of the Budget and Finance Committee
City Clerk
City Hall, Room 395

REPORT BACK ON DRAFT GENERAL BANKING SERVICES REQUEST FOR PROPOSAL

Dear Honorable Members:

Further to the direction (Council File No. 17-1259) of the Budget and Finance Committee (Committee) on November 6, 2017, the Office of Finance (Finance) is responding to various questions posed by Committee regarding the draft General Banking Services Request for Proposal (RFP). Following is discussion of the issues identified by the Committee for further consideration.

Term

The RFP provides a contract term of five years with an option to renew annually for up to an additional five years. The reason for this term is primarily due to the time and expense associated with transferring banking services.

Once an agreement is finalized between the City and any prospective financial institutions that prevail in the RFP process, there will be a considerable amount of work to be performed in migrating and establishing accounts to new bank platforms, testing file transfers between the City and bank financial systems, establishing and testing security protocols, and training City staff on new bank systems. Employee and contractual resources will be expended by not only Finance, but by every individual department utilizing banking services.

It could take at least a year to functionally transfer all accounts and services to a new bank platform. The proposed five-year term would allow sufficient time to responsibly migrate City accounts to a new bank platform, time to evaluate the contractual relationship, and time to pursue potential service enhancements benefiting the City.

Engaging in a banking relationship with the City also incurs costs for the bank which will seek to recover its own implementation costs. Finance believes that a longer term allows the banks to better justify their startup costs and thereby lower the overall cost of banking services to the City.

Weighting of Social Responsibility

Current Scoring
As drafted the RFP will be evaluated and scored in three phases as shown below.

Phase 1 – Written Proposal Evaluation	**Phase 2 – Interview Evaluation**	**Phase 3 – Compensation Evaluation**
Organizational Capability 30 points Scope of Services 50 points Social Responsibility 20 points	Business and Technical Capability 30 points Service Enhancements 25 points Implementation Plan 15 points Social Responsibility 20 points References 10 points	Pricing and Compensation 25 points
Respondents with a total score of at least 70 points will be invited to participate in the second phase of scoring.	A weighted score of Phase One (70 percent) and Phase Two (30 percent) will be established prior to advancing to Phase Three Scoring.	The points from Phase Three scoring will be added to the weighted score of Phases One and Two Scoring to determine final ranking of bidders for award in each individual Service Category.

As part of the Committee's consideration of the RFP, Councilmember Martinez's letter to the Committee dated November 6, 2017 requested a recalibrated scoring structure which places equal value on Social Responsibility as it does on Organizational, Business or Technical Capability.

After considering the elements of the RFP, Finance believes it is not in the best interest of the Treasury or the City to increase the Social Responsibility score value within the draft framework relative to the Organizational, Business, or Technical elements of the RFP because such an action is incongruous with the City Treasurer's fiduciary mandate set forth in California State law.

Fiduciary Requirements
Los Angeles City Charter Section 301 and California State Government Code Section 53600.3 establish the City Treasurer as the trustee of all money deposited in the City Treasury. Furthermore, California Government Code Section 53600.3 mandates that the City Treasurer, as a trustee of public funds, is subject to the prudent investor standard. When managing public funds, the City Treasurer must act with care, skill, prudence, and diligence under the prevailing circumstances (such as the economic conditions and anticipated needs of the City), in such a way that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character (such as other municipal

Treasurers acting as trustee's for their respective agency funds), to safeguard the principal and maintain the liquidity needs of the City.

California Government Code Section 53600.5 also directs that the City Treasurer, when managing public funds, consider three objectives as the trustee of the City's funds: 1) the primary objective shall be to safeguard the principal of funds in the City Treasury; 2) the secondary objective shall be to meet the liquidity needs of the City; and, 3) the third objective shall be to achieve a return on the funds under the Treasurer's control.

California Government Code Section 53649 also states that the Treasurer is responsible for the safekeeping of money in his or her custody and shall enter into any contract with a depository relating to any deposit which in his or her judgment is to the public advantage.

Finance believes that placing a higher evaluation score on the Social Responsibility elements of the RFP relative to the financial, organizational and product capabilities of a financial institution dilutes the City's application of the prudent investor standard. While Finance recognizes the importance of a firm's commitment to social responsibility, the primary consideration should be given to a financial institution's strength to ensure the safety of City deposits into such an intuition, and the financial institution's organizational capacity and business solutions to help Finance satisfy the daily and long term liquidity needs of the City.

California law takes into consideration the financial strength and stability of banks. California Government Code Section 53635.8 requires that any private sector entity used by the City be capitalized at a sufficient level and insure the full amount of each deposit by the Federal Deposit Insurance Corporation.

California Government Code Section 53635.2 requires a minimum overall "satisfactory" rating in its most recent evaluation by an appropriate federal financial supervisory agency of a financial institution's record of meeting the credit needs of California's communities to be eligible to receive City funds. However, California law does not establish standards or requirements for social responsibility.

<u>Other Jurisdictions' Weighting of Social Responsibility</u>
Finance investigated how other agencies applied score values for social responsibility in their respective RFPs for bank services. The City identified a few agencies that have provided numerical weight to social responsibility as part of its RFP score criteria. In each instance, the value placed on social responsibility (City of Seattle – 15 percent, West Hollywood – 15 percent, City of Berkeley – 10 percent, and the City and County of San Francisco – 5 percent) was lower than what the City is proposing at a net weight of 16 percent and many others had no scoring provision for Social Responsibility whatsoever. In considering how other agency Treasurers applied score values for social responsibility, Finance believes that adding more weight to social responsibility as drafted in the City's RFP could be construed as incompatible with the prudent investor standard required by California State law.

However, Finance can offer an alternative scoring arrangement that maintains the City Treasurer's fiduciary responsibilities while providing greater weight to Social Responsibility.

Alternative Scoring Proposal
An alternative scoring proposal that may provide greater weight to Social Responsibility while complying with the City's fiduciary mandate would be to restructure the scoring as follows.

Phase 1 – Organizational Capability	**Phase 2 – Social Responsibility**
Financial Strength 30 points Customer Service 10 points References/Experience 5 points Implementation Plan 5 points General Requirements 5 points Services/Products 30 points Cost 15 points	Social Responsibility 30 points Comprised of: • Enforcement Actions 15 points • Community Lending, Investing and Banking Services 15 points
Respondents with a total score of at least 70 points will be invited to participate in the second phase of scoring.	The Social Responsibility score would be converted to percent and added as a percentage of the Organizational Capability score to calculate a Total Score.

Under this scoring system, financial institutions will need to first establish their capability to provide services to the City and once that threshold is met, the Social Responsibility component can be used to differentiate among qualified bidders. For demonstration purposes, a bank that scores 100 in Phase I could achieve a total score ranging from 130 (highest possible Social Responsibility score) to 100 (lowest possible Social Responsibility score) while a bank that scores 90 in Phase I could achieve a total score ranging from 117 to 90; thereby creating scenarios where a capable but lower scoring bank in the first phase could surpass a higher scoring bank within a reasonable range on the basis of Social Responsibility.

Composition of Social Responsibility Criteria

The Committee requested that Social Responsibility scoring be structured in such a way as to emphasize "bad actors."

First, there are several pass/fail requirements that a Respondent must meet:

1. Compliance with the City's Responsible Banking Ordinance
2. An overall national and state Community Reinvestment Act rating of at least "Satisfactory"
3. Compliance with the City's requirement regarding Consumer Adverse Practices (see same named section of this report below)

Second, there are several areas subject to scoring including:

1. Enforcement Actions (see Reporting of Enforcement Actions section of this report below) which emphasizes negative behaviors (or lack thereof) by financial institutions
2. Community Lending, Investment and Banking Services which emphasize empirical banking practices within the City
3. Corporate Citizenship which identifies philanthropy, charitable giving and narratives for the Respondents to tout their good practices.

In discussing concerns of how these areas would be balanced in the scoring, some valid points were made particularly with regard to weighing "good" activities versus "bad" activities. Accordingly, Finance is recommending a change to the composition of the Social Responsibility category such that scoring is separated equally between (1) Enforcement Actions and (2) Community Lending, Investment and Banking Services. The Corporate Citizenship component will be removed as it is less empirical and relies largely on the Respondents' narrative.

RFP Evaluation Panel

In keeping with the fiduciary mandate of the City Treasurer, Finance believes the RFP evaluation committee should be composed of those members best able to evaluate the ability of Respondents to provide the City's required banking services. As such, Finance will assemble an evaluation committee composed of Finance staff, along with representatives of other City departments, including proprietaries, and will also seek participation from a government treasury professional representative from another jurisdiction.

It was also suggested that "social responsibility" organizations serve as References for scoring purposes. This is not recommended by Finance as the intent of References is to assist in evaluating the Respondents' ability to meet the City's general banking services requirements and not intended to address Social Responsibility which is separately scored.

Consumer Adverse Practices

The Committee requested further definition of predatory practices and its application in the RFP. In researching the disallowance of predatory practices by banking institutions, Finance has determined that the term "predatory" is most readily defined in the context of a regulatory environment. As such, Finance is relying on regulatory agencies in applying this requirement and proposes the below language to be incorporated to the RFP.

A Respondent to this RFP must certify that it does not engage in illegal predatory consumer adverse practices nor base evaluation, promotion, discipline, or compensation of any employee on illegal predatory consumer adverse practices within the City. The determination that a banking practice is predatory or illegal shall be based on findings made by appropriate government regulatory agencies, such as the Consumer Financial Protection Bureau, and courts of law.

The Committee also commented on the implications of disallowing sales goals by banks. Finance has not observed that provision in other jurisdictions' RFPs or Responsible Banking Ordinances (RBO), which tend to limit the definition of predatory to lending practices. Disallowance of sales goals may result in no or limited eligible bidders qualified to provide the City's general banking services.

Reporting of Enforcement Actions

The Committee requested that Finance refine the language requiring reporting of investigations and enforcement actions. Finance has drafted the below language intended to define the instances in which a financial institution would be required to report regulatory actions to the City.

To the extent permitted by law, respondents must provide a statement disclosing any enforcement action undertaken by the Consumer Financial Protection Bureau, Department of Justice, Federal Deposit Insurance Corporation, Federal Reserve Board, National Credit Union Administration, Office of the Comptroller of the Currency, U.S. Securities and Exchange Commission, or any applicable state banking regulatory body (such as the California Department of Business Oversight) against the Respondent in the past five (5) years. In the disclosure statement, the Respondent shall provide a description of the enforcement action, reason for enforcement action, date of enforcement action, the enforcing agency, measures taken by the financial institution to address or resolve the cause of the enforcement action, and current disposition of the enforcement action (supplemental information regarding regulatory enforcement actions may be included as an exhibit to the submittal).

Furthermore, during the period from submission through notification of award of this RFP, Respondents are required to disclose to the City, in the same manner as required above, any public open investigation or enforcement action undertaken by same regulatory agencies against the Respondent within ten (10) days after an action is taken or a fine or penalty is imposed. Same provision will also apply during the life of the agreement with the City.

Finance believes the language to be clear and reasonable while achieving the City's goals in scoring the RFP and in continuing to monitor the regulatory activity involving the City's banking partners. Similar provisions exist in some other RFPs observed by Finance with the key being to define enforcement actions as determined by Federal and State regulators.

Contractual Accountability Measures

The Committee also requested that Finance identify accountability measures that can be worked into the contract and whether there could be a penalty or fine for any consumer adverse action by a bank vendor.

The City may terminate for convenience any contractual agreement with a bank pursuant to the termination language in the City's Standard provisions for City Contracts (PSC-9

Termination). However, if the City chooses to exercise this option, the City would be responsible for all costs associated with acquiring these same services from another vendor. In such an instance, the City would have to balance its desire to terminate an agreement for convenience against the costs and disruptions to the City's bank services and financial operations resulting from such a termination.

The City may terminate any agreement with a bank for cause pursuant to the termination language set forth in the City's Standard provisions for City Contracts (PSC-9 Termination), which would be incorporated into any contractual agreement with a bank. In the event the City terminates for cause, the City may procure services similar in scope and level of effort to those so terminated, and the contractor shall be liable for costs and damages including any excess costs for such services.

Finance will also incorporate language into its agreement with the successful Respondents to the RFP that would allow the City to obtain compensatory damages for any financial services that result in monetary loss to the City. Losses could occur from such activities as delays in processing revenue deposits or delays in processing City payments to meet its financial obligations.

However, the City could not apply a penalty or fine for any consumer business practices the City deems inappropriate by a City bank services vendor. Such actions by the City could be construed as a regulatory action, and the City is not a financial services regulatory agency, especially if these actions are outside the scope of any contractual agreement between a bank vendor and the City.

Other Cities' Responsible Banking Ordinances

Finance has compiled a summary matrix (see Attachment) of ten other jurisdictions' Responsible Banking requirements as requested by the Committee. The attached matrix notes several of the elements pondered by the Committee that are found in these agencies' respective municipal codes. Finance identified the following notable trends:

- Nearly all agencies require the disclosure of a CRA rating and the lending information analogous to the lending disclosures required by Community Reinvestment Act of 1977 (12 U.S.C. § 2901, *et seq.*).

- At least six agencies address predatory lending practices by a financial institution that maintain deposits by the respective agencies in this review by precluding the deposit of funds into institutions that have been the subject of a court judgement that they have engaged in predatory lending practices to their respective constituents.

- Some agency ordinances establish a community reinvestment review committee to evaluate the financial institution to its peers, review the bank's community reinvestment plan, and evaluate data and information submitted by a financial institution wishing to accept municipal deposits and contracts for banking services.

- Most agencies require the depository institutions to provide an annual plan, and in some instances a two-year plan, for community involvement and reinvestment activities by the depository agency.

Recommendation

It is recommended that the Budget and Finance Committee note and file this transmittal.

If there are any questions, please contact Todd Bouey, Assistant Director of Finance, at (213) 978-1776 or by e-mail at todd.bouey@lacity.org.

Sincerely,

Claire Bartels

Claire Bartels
Director of Finance / City Treasurer

Attachment

cc: Miguel Sangalang, Deputy Mayor, Budget and Innovation, Mayor's Office

ATTACHMENT

RESPONSIBLE BANKING ORDINANCE
MULTI-AGENCY COMPARISON

Agency	RBO	Community Reinvestment Plan	Non-Retaliatory Practices	Predatory Lending	Disclosure of Lending Information	Non-Discrimination	Community Reinvestment Committee	Enforcement Action	CRA Rating	RFP Selection Criteria	Other
Los Angeles	√		♦	♦	√			♦	√	♦	
Boston	√	√	√	√	√	√	√		√	√	RBO requires a Pledge from an authorized official from the financial institution that it: Supports Community Reinvestment, refrains from any steps in foreclosed residential properties other than for "just Cause", established whistleblowing mechanisms, makes a best effort to abide by State usury law setting maximum credit card interest rate at 18%, not to engage in predatory lending, redlining activities, or discriminate in lending activities.
Cleveland		√		√	√		√		√		
Minneapolis	√	√			√	√			√	√	
Monterey	√	√		√	√					√	RBO requires financial institutions to provide a two-year plan for loans and services and to describe how it will match or exceed peer CRA performance.
New York				√			√				NYC Responsible Banking Act struck down by Federal Court in 2015 ruling it preempted Federal and State Banking Laws.
Philadelphia		√		√	√		√				City has a code addressing the prohibition against predatory lending practices (Philadelphia Code, Title 9 *Regulation of Businesses, Trades and Professions* , Chapter 9-2400 *Prohibition Against Predatory Lending Practices*).
Pittsburgh	√	√		√	√		√		√	√	Municipal ordinance establishes score criteria for responsible banking and neighborhood reinvestment criteria.
San Diego	√	√		√	√				√	√	
Seattle	√	√			√				√	√	Requires that Socially Responsible Banking performance as a factor be worth at least 15% of a total point value determining a winning bid. Requires a CRA rating of "Outstanding" in bid acceptances.

√ Addressed in the respective agency municipal or administrative code.
♦ Items in consideration for Los Angeles' Responsible Banking Ordinance.