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**OFFICE OF THE
CITY TREASURER**

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February 22, 1991
I00131DC.DCC

Budget & Finance Committee
Sacramento, California

Honorable Members in Session:

SUBJECT: PAYMENT FOR CITY BANKING SERVICES

SUMMARY

This report requests that the Budget & Finance Committee receive and forward the attached investment report regarding the new payment method for City banking services implemented by the City Treasurer.

BACKGROUND

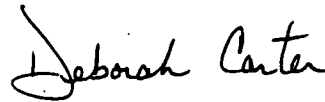
"See the attached report to City Council".

Budget & Finance Committee
Payment for City Banking Services
February 22, 1991

RECOMMENDATION

The attached report informs the City Council of a new payment method implemented by the City Treasurer's Office effective January 1991 which will result in annual additional revenue to the City of approximately \$121,000.

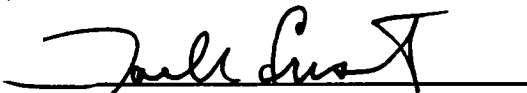
Respectfully submitted,



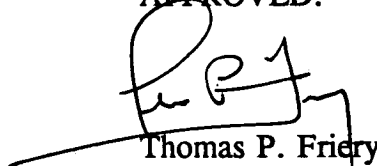
Deborah Carter
Investment Officer II

RECOMMENDATION APPROVED:

APPROVED:



Jack R. Crist
Deputy City Manager



Thomas P. Friedry
City Treasurer

March 5, 1991

Contact Person:
Deborah Carter, Investment Officer II
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I00131DC.DCC
February 22, 1991

City Council
Sacramento, California

Honorable Members in Session:

SUBJECT: PAYMENT FOR CITY BANKING SERVICES

SUMMARY

This report provides information to the City Council regarding the payment for City banking services. The new payment method implemented by the City Treasurer's Office effective January 1991 will result in additional revenue to the City of approximately \$121,000.

BACKGROUND

The City Treasurer's Office has changed the way that City banking services are paid to the bank. In the past, most municipalities have paid for banking services through compensating balances. However, the increasingly competitive nature of the banking industry has created new competitive options and services. An overview of the City's banking service needs and a discussion of each payment option follows.

The annual fee for the City's banking services is approximately \$464,000 per year. This fee covers the following services:

<u>Service</u>	<u>Cost</u>
• Armored Car	\$192,000
• Lockbox (Utility payments)	85,000
• General Demand Account	27,000
• Safekeeping & Custody	<u>160,000</u>
Total	\$464,000

The three methods currently being used by public agencies to pay for banking services are compensating balances, sweep balances or direct payment of services. Each method has advantages and disadvantages and is discussed below.

The **compensating balance** option is less time consuming for staff to monitor. It can be compared to a personal checking account which shows the income, disbursements, and remaining balance (uninvested cash) available. On a daily basis, cash is left in the bank account and the earnings are used to offset the cost of the City's banking services. The amount of the balance necessary to pay for services is dependent on the current earnings rate and the total cost of services. The two primary disadvantages of this payment method are the reserve requirements and the Federal Deposit Insurance Corporation (FDIC) fees. There is currently a twelve percent (12%) reserve requirement for demand deposits which is subtracted from earnings left in the bank to pay for services. Also, the FDIC charges a banking service fee based upon the average account balances left in the demand account, which further increases the City's costs. While this method is less time consuming, it is the most costly plan.

Although the **sweep balance** option requires additional staff time to monitor, there are significant revenue benefits. Each day after all the income and disbursements have been accounted for, any uninvested cash balance is swept into the bank's government money market fund. As a result, the account balance is zeroed out each day. Since there is no balance, there is no reserve requirement and only minimal fees are due to the FDIC. The monies previously needed to offset the reserve requirement and FDIC fees can then be used to generate this additional revenue.

To effectively implement the **direct payment** of all banking services option it would be necessary to keep a minimum cash balance. However, staff can not project exactly how much income and disbursements will be posted to the City's bank account, thus uninvested cash balances would result. It may be possible to combine the sweep balance feature with the direct payment method to prevent over-drafting of the bank account. However, staff has not completed an evaluation of this option.

FINANCIAL

As discussed in the background, there are positive and negative benefits to all of the options mentioned. However, the financial benefit to the City was the primary reason for the implementation of the sweep balance option.

The current \$121,380 annual additional revenue is detailed on Attachment 1. The direct benefit to the General Fund is approximately \$29,000. Currently, the margin between money market investments and U.S. Treasury Bills are narrower than would be expected in a more normal interest rate environment. Therefore, the City Treasurer believes this earnings estimate is relatively conservative. To make certain the sweep procedure operates properly, the Investment Officer responsible for City investments is currently monitoring the bank balance. Following a phase in period, these routine bank account monitoring duties should be performed by an investment technician which would allow the Investment Officer to concentrate on City Investments.

POLICY CONSIDERATIONS

None.

MBE/WBE

None.

RECOMMENDATION

This report is provided for informational purposes only and does not require City Council action.

Respectfully submitted,

Deborah Carter

Deborah Carter
Investment Officer II

APPROVED:

Thomas P. Friery

Thomas P. Friery
City Treasurer

APPROVED FOR COUNCIL INFORMATION

Walter J. Slipe
City Manager

Contact Person:
Deborah Carter, Investment Officer II (916) 449-5168

March 12, 1991:

CITY OF SACRAMENTO 1991 BANKING SERVICES

	<u>COMPENSATING BALANCES</u>	<u>SWEEP BALANCES</u>
Collected balance	9,000,000	-0-
Less:		
12% Reserve requirement	(1,080,000)	<u>-0-</u>
Earnings Balance	7,920,000	9,000,000
Est. Earnings Rate	6.10% ¹	6.60% ²
Monthly earnings rate	39,708	48,822
Less:		
FDIC Charge	(1,057)	(56) ³
EARNINGS AVAILABLE TO OFFSET BANKING FEES	38,651	48,766
ANNUALIZED EARNINGS	\$463,812	\$585,192
ANNUALIZED NET BENEFIT OF SWEEP BALANCE	<u>\$121,380</u>	

¹ Estimated earnings rate of the 90-day U.S. Treasury Bill.

² Estimated earnings rate of the Pacific Horizon Government Fund at Security Pacific Bank.

³ The FDIC charges a fee based upon the average bank account balance. Based on an earnings balance of \$7.9 million, the FDIC charge would be \$1,507. While the earnings balance on the sweep account is \$9.0 million, the actual account balance is closer to zero. Therefore, the resulting FDIC charge would only be about \$56 per month.