Deferred Compensation Plan
BOARD REPORT 14-28

Date: July 2, 2014

To: Board of Deferred Compensation

From: Staff

Subject: Selection of Contractors for the FDIC-Insured Savings Account Option

Recommendation:
That the Board of Deferred Compensation Administration:

a) Approve the selection of Bank of the West and East West Bank as providers for the City of Los Angeles Deferred Compensation Plan FDIC-Insured Savings Account;

b) Instruct staff to draft a proposed contract for each of the above selected providers and authorize the Board Chairperson to execute the contracts, subject to agreement between the City and contracted providers as to all applicable terms and conditions;

c) Find that the use of competitive bidding for a third provider would be undesirable and impractical and therefore direct staff and the Plan's investment consultant to perform a search for a third provider; and

d) Direct staff to seek City Council authorization of any needed extensions required for this option's incumbent providers if new contracting deadlines are unable to be met, and authorize the Board Chairperson to execute any necessary contract amendment(s) with those providers to extend the contract(s).

Discussion:
This report contains recommendations related to the selection of providers for the Deferred Compensation Plan FDIC-Insured Savings Option pursuant to the Plan's recently issued Request for Proposal. Two proposals were received, both of which have been determined by staff and the consultant to be viable institutions. Since this option is structured to have three underlying providers, additional steps will need to be taken to address the need for a third provider. This report will first address the RFP results and recommendations, and then address the matter of finding a third provider.

I. Background

The FDIC-Insured Savings Account is an option in the Deferred Compensation Plan's core investment menu. The foremost objective for this option is capital preservation. As indicated in the Plan's Investment Policy Statement (IPS), this option is intended to have three underlying providers with equal allocations of the total asset pool, unless the Board adjusts such allocation based on institutional viability and/or interest rate differentials.

Currently, the option's providers and respective allocations are:

1) Bank of the West (50% of total asset pool)
2) Bank of America (25% of total asset pool)
3) City National (25% of total asset pool)

The current five-year contracts for these providers will expire on **September 30, 2014**.

II. Request for Proposal and Recommended Providers

On April 8, 2014, a Request for Proposals (RFP) for potential FDIC-Insured Savings Account providers was released. On May 1, 2014, a mandatory pre-proposal conference was held. The following firms attended (in alphabetical order):

1) Bank of America
2) Bank of the West
3) East West Bank
4) JP Morgan
5) NY Life
6) Wells Fargo

It should be noted that over six months ago incumbent provider City National Bank indicated to staff that it was no longer interested in providing these services and would not be participating in future procurements. Additionally, while RFP responses were still pending, incumbent provider Bank of America indicated it would not be responding to the RFP.

Proposals to the RFP were due on June 13, 2014. Proposals were received from the two following firms:

1) Bank of the West
2) East West Bank

With the assistance of the Personnel Department's Administrative Services Division and the Plan's investment consultant, Mercer Investments, respondents were initially evaluated for:

a) *Contracting Viability* – The ability to comply with general City contracting requirements.
b) *Operational Viability* – The ability to work consistently with one another and the Plan's record-keeper, Great-West Retirement Services, with respect to interest rate crediting and reporting.

Upon ensuring that the respondents met the above minimum requirements of the RFP, evaluation of the service components was completed by the Plan's investment consultant, Mercer Investments Consulting ("Mercer"), based on the review criteria adopted by the Board for this RFP.

The Review Criteria and summary scoring are indicated as follows:

Category - Rating Factors	Scale	East West Bank	Bank of the West
Financial Strength	**200.00**	**104.17**	**178.10**
➢ Assets, deposit base, and equity	75.00	37.50	65.63
➢ Credit ratings	50.00	16.67	37.50
➢ Key ratios	75.00	50.00	75.00
Relevant Experience and Service	**40.00**	**15.00**	**27.50**
➢ Number of retirement plan clients	15.00	0.00	7.50
➢ Public Sector Clients	10.00	5.00	5.00
➢ Client service capabilities	15.00	10.00	15.00
FDIC Insured Product Characteristics	**200.00**	**200.00**	**143.75**
➢ Product viability in DC plan	50.00	50.00	50.00
➢ Competitiveness of interest rate structure	75.00	75.00	18.75
➢ Collateralization complies with regulations	25.00	25.00	25.00
➢ Presence of additional fees	25.00	25.00	25.00
➢ Capacity to accept Plan deposits	25.00	25.00	25.00
Accounting Capabilities	**60.00**	**60.00**	**60.00**
➢ Interface With Record-Keeper	35.00	35.00	35.00
➢ Reporting	25.00	25.00	25.00
TOTAL-->	**500.00**	**379.17**	**409.38**

The attached report from Mercer contains its review and analysis of each bank's minimum required qualifications and quality of proposed service delivery. Mercer's report indicates that, "while we would prefer to see a greater number of respondents, larger institutions proposing, and also higher proposed interest rates, the current demand for deposits on the part of major banks is very limited." With respect to scoring, East West Bank received lower marks than Bank of the West in the Financial Strength category due to its size, and Bank of the West received lower marks in the competitiveness of crediting rates category because its proposed methodology, at today's rates, is less than half the rate provided by East West Bank.

The broader interest rate environment is, in both staff and the consultant's view, the fundamental driver of low rates and lack of interest from the provider community. Nevertheless, Mercer indicates, and staff further concurs, that "both banks are viable providers for the Plan." Based on this, staff and Mercer recommend that the Plan select Bank of the West and East West Bank as underlying providers for the FDIC-Insured Savings Account option.

III. Third Provider

The FDIC-Insured Savings Account option is structured to include three underlying providers. This structure was developed to expand the amount of FDIC-Insurance coverage available to participants and also to provide options for the Plan to shift assets in the event concerns arose as to the institutional viability of an underlying provider. The Board created this structure in 2009 following the FDIC-brokered acquisition of former provider Washington Mutual Bank.

The Board issued an RFP for this option in 2009, seeking three providers. Only one response was received. As a result, the Board directed staff and the consultant to conduct an independent search process (no re-issuance of the RFP) to identify viable providers. Ultimately three providers were identified and contracted with.

A similar situation has arisen in this instance, as only two viable providers are available pursuant to this RFP. The lack of interest from the provider community in competing for this contract is likely related, as it was in 2009, to an unusual set of credit, monetary policy, and interest rate conditions. Savings deposits of this nature may be viewed by some institutions as representing liabilities or not in alignment with the institution's strategic interests.

Irrespective of the underlying reasons, with the incumbent contracts expiring 09/30/14, the Plan should move as expeditiously as possible to identify a third provider. City governance documents provide contracting authorities certain flexibility in searching for service providers when the normal RFP process is not meeting the City's needs. The City's Charter Code, Section 371(e)(10) provides exemption from the bid process for:

> *…contracts (including without limitation those, as determined by the contracting authority, for the performance of professional, scientific, expert, technical or other special services), where the contracting authority finds that the use of competitive bidding would be undesirable, impractical or impossible or where the common law otherwise excuses compliance with competitive bidding requirements.*

The City's Administrative Code, Section 10.15(a)(10), further provides:

> *…the term "undesirable" shall mean and include only such situations in which the nature of the subject of the contract is such that competitive bidding would work an incongruity or be unavailing or would not produce an advantage, with sole reference to the public interest and in light of the purposes to be accomplished.*

Similar to the circumstances the Plan encountered in 2009, staff finds that reissuing the RFP is impractical and undesirable because the RFP was properly noticed and resulted in an insufficient number of responses, and there is no indication that reissuing it would produce a dissimilar result.

Conducting an expedited search for a third provider and using the successful independent search approach previously utilized in 2009 would be in the best interests of the Plan and its participants, as it would move the Plan more swiftly towards provider stability (an element that is especially important for this option, which participants look to for stability and capital preservation). The search process would be based on an identical set of criteria adopted by the Board for the RFP, and would be transparent and inclusive. Any selected provider would still be required to comply with the City's general contracting requirements.

Based on this, staff therefore recommends that the Board find the competitive bidding process would be impractical and undesirable in identifying a third provider and direct staff to work together with the Plan consultant to conduct an independent search that allows identification of viable institutions strictly in accordance with the search criteria utilized in the RFP. This will allow the Board to identify and select a competent third provider in a manner most beneficial to Plan participants and ensure stability and quality of the option. If the Board approves this recommendation, staff and the consultant will return at the Board's August meeting with the results of its review and recommendation for a third provider.

IV. Authority to Request Contract Extensions (if needed)

If the Board adopts staff's recommendation to select Bank of the West and East West Bank at this meeting, staff will have approximately 11 weeks to execute contracts for these two providers. If the Board selects a third provider at its August 19 meeting, staff will have 6 weeks to execute a contract for that provider. These are challenging timelines and meeting them will be impacted by the complexity of issues that may arise between the City and the vendors regarding contract terms and conditions. In the event that resolution of these issues requires additional time, staff is requesting authority from the Board to request that the City Council provide authority for extending one or more of the existing contracts. Staff would only proceed with this request upon clearer indications that contracting deadlines will not be met. Staff further recommends that the Board authorize the Board Chairperson to execute any necessary contract amendment(s) with these providers to extend the contract(s).

VI. Interest Rate Differential and Provider Allocations

The Plan's Investment Policy Statement (IPS) provides that normally the allocation of assets will be split evenly, by thirds, between the three providers of the FDIC-Insured Savings Option. However, the IPS further provides the Board with flexibility to permit a larger allocation to one of the bank providers should that provider offer a rate with a significant difference over the other providers.

Currently, Bank of the West has been allocated 50% of the total asset pool due to having a significantly higher interest rate than the other two providers, which are allocated 25% each. However, with the rates proposed by Bank of the West and East West Bank pursuant to the 2014 RFP, that rate differential no longer exists. As such, once the Plan has identified all of its providers, and assuming no significant rate differential from the third provider, staff will recommend that the allocation be returned to the original IPS structure. This issue will be reviewed and addressed in more detail at the Board's August meeting.

Submitted by: __________________________________

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