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# Annual Conference

OCTOBER 27-30, 2013 | LAS VEGAS

ORIGINAL → ESSENTIAL → UNBIASED → **INFORMATION**

## Understanding the Changing Landscape of Account Analysis

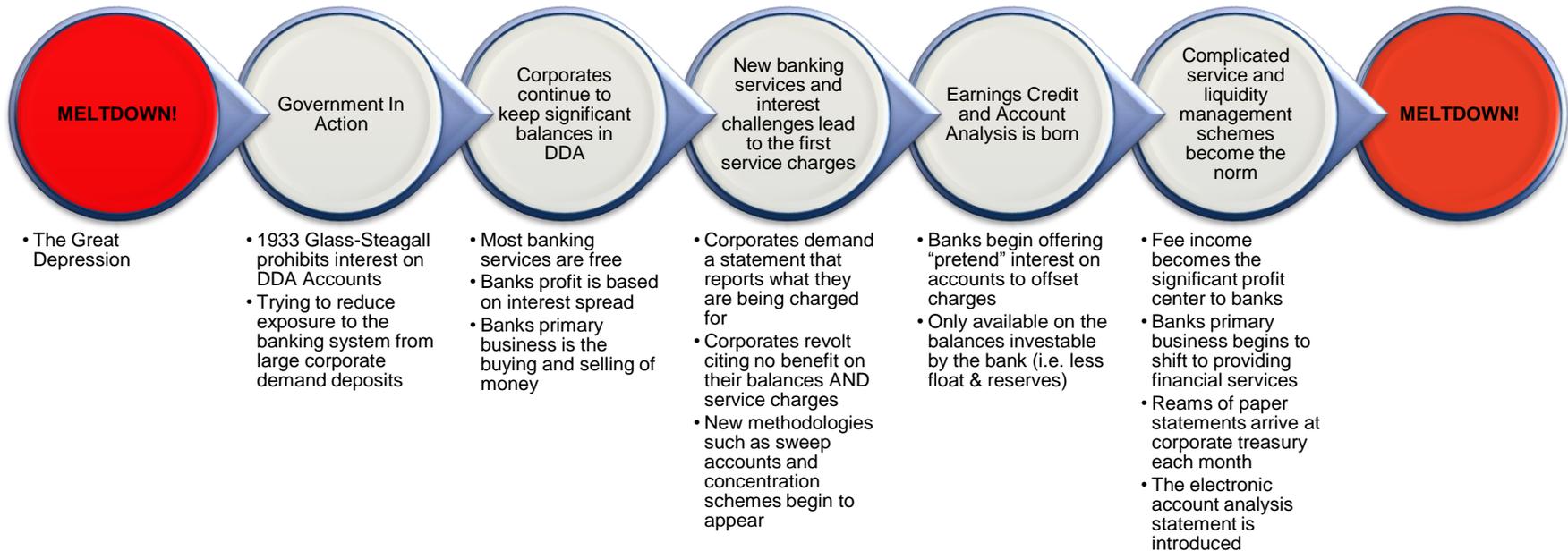
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# Take Aways

- **Understand the How's and Why's of Account Analysis from the corporate treasury point of view**
- **Understand the pressures on bank fees that have developed as a result of the financial crisis**
- **Understand the need to analyze and monitor your bank fees**

# The History of Account Analysis



# Account Analysis Is:

- **A bill for services from a vendor**
- **A method to gain value from balances in transaction accounts**
- **A valuable reporting tool**
  - Every balance, every rate, every price, volume & charge for every service
  - For every account
  - For every bank
  - Forever
  - *If you receive the 822 or BSB electronic statement*
- **100% Negotiable**

# The BSB: A Global Solution

- An international services billing statement in an ISO 20022 standard, electronic format known as camt.086
- Used to transmit bank balance, service charge, **tax, currency** & adjustment data from a bank to its commercial customers or to another bank
- Designed to address global coverage of electronic account analysis (EAA) Identical in data content to the concept proven US 822 standard but with the addition of **tax & currency** data
- Uses billing codes (Global AFP Service Codes) to standardize identification of bank services.
- Maintains all the 822 data content
- Provides a treasure trove of MIS data, payments mix and business vitality metrics
- ISO:[http://www.iso20022.org/payments\\_messages.page#payments\\_catalogue\\_bsb](http://www.iso20022.org/payments_messages.page#payments_catalogue_bsb)

# Account Analysis is Special Because:

- **The vendor (your bank) can typically take the fees levied on the bill straight out of your account – auto debit**
- **The “interest” that you receive on only part of your balances is pretend**
- **The fees paid for the same service vary greatly across companies, banks and within your own bank**

# Recent Events in Account Analysis

## Meltdown

- Devastation of banks' balance sheets
- Too Big to Fail
- Counterparty risk we never imagined
- Lending vapor lock

## Government in Action

- Bailout Bill
- TARP
- Interest on Reserves
- Changes in Consumer Fees
- FDIC Changes
- Dodd – Frank – Durbin
- Hard Interest

# What is the New Account Analysis?

What does the financial crisis have to do with account analysis?

Account Analysis is the last step in the monthly relationship with your partner banks



Everything you do with your banks affects account analysis



The economic & regulatory environment affects your account analysis



Everything on account analysis is negotiable

# The New Account Analysis

Interest on Reserves

FDIC Fees

Consumer Banking Fees

Interest on Demand Deposit

Relationship Based Pricing

# Interest on Reserves

## What does it mean?

- The Federal Reserve uses the Fed Funds Rate to implement monetary policy
- Traditionally, this has been done through the open market using securities held by the Fed
- As part of the original bailout bill, the Fed began paying interest to banks on their required and excess reserves

## Why did they do it?

- In the “cash hoarding” scenario since the financial crisis, the Fed had difficulty actually maintaining their target Fed Funds Rate
- By paying interest on the reserves held by banks, they can in effect set a floor below which banks won't lend money to each other giving better control to short term rates

# Interest on Reserves

## What does it have to do with account analysis?

- For years, we have seen our earnings credit balances reduced by the required reserves that the banks must keep
- We have been told that we can't have earnings on these balances because the bank gets no benefit from them
- Now the banks ARE getting benefit from OUR balances held in reserve... we should too!

## What impact has it had?

- Many banks have simply eliminated the reserve reduction from their analysis calculations
- Currently, the Fed Funds Rate is essentially zero and earnings credit rates are very low, so this hasn't had much impact...so far

# Interest on Reserves

What does the future hold?

- Interest rates are bound to increase and as that happens, that 10% reduction in earnings will become real again

Do you know how each of your banks is handling interest on reserves?

- Do you know the two ways reserves can impact your account analysis?
- Do you know how each of your banks determines the rate they give you?

# Changes to Consumer Bank Fees

There have been a number of new regulations put in place designed to keep banks from “overcharging” consumers

- NSF opt-out
- Credit card rate limitations
- Limits on consumer bank fees
- Swipe Fees
- Debit Card
- Market pressure on payment methods

What does that have to do with account analysis?

- The overall fee income stream of banks has been reduced by tens of billions annually...they will need to recoup this revenue from somewhere

# FDIC Changes

The banking crisis has brought so many changes to how the FDIC operates that we could spend an entire day talking about them

- Coverage increased to \$250,000
- Unlimited coverage with TAGP
- TAGP opt-out
- Assessment prepay
- Special assessments
- Dodd-Frank
- Unlimited Coverage
- Changes in assessment calculations
- What's in a Name?

# FDIC Changes

## Unlimited FDIC Insurance

- Dodd-Frank authorizes unlimited FDIC coverage
- Covers only non-interest bearing accounts
- Unlimited coverage by all FDIC insured participating banks
- No special assessments for coverage

# FDIC Changes

The changes in FDIC fees, and how they are passed through account analysis has already been dramatic

- Most of us felt the more than 200% increase that happened in FDIC fees in the past couple of years
- While the fees have stabilized somewhat in the past year, the methods used to determine your FDIC fees remain a mystery at most banks

Through it all, we have been able to count on the basic premise that our FDIC fees were basically just a pass through of the charges our banks were paying to insure those balances

# FDIC Changes

## That Has Changed

- Under new FDIC rules contained in Dodd-Frank, the method used to calculate what a bank pays for coverage is no longer just a function of the balances that are covered
- Banks are faced with many additional changes and costs associated with FDIC coverage

## What Does it Mean?

- There is no way to be sure that we are getting charged “our fair share” for FDIC coverage on our accounts.
- What about our accounts moving to interest bearing status

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# Handling FDIC in the New World

Lets look at FDIC fees from a new direction

- On account analysis FDIC appears as a service line
- What are we buying for that fee?
- We are buying insurance coverage for one of our company's assets
- *Do you pay your doctor for his malpractice insurance?*

# Handling FDIC in the New World

If we look at the FDIC from our point of view:

- We put ourselves in a position where we can negotiate from
- We put ourselves in a position where we can watch for errors
- We eliminate any complex explanations we get from our banks

# The FDIC Ratio

By looking at FDIC fees for what they are, we can develop the ratio of the total cost for the coverage vs. the total balance covered

There are a number of variables that need to be evaluated, but with the right formula, we can accurately compare our banks for the cost of FDIC coverage for each dollar we have on deposit.

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# Interest on Demand Deposit Accounts

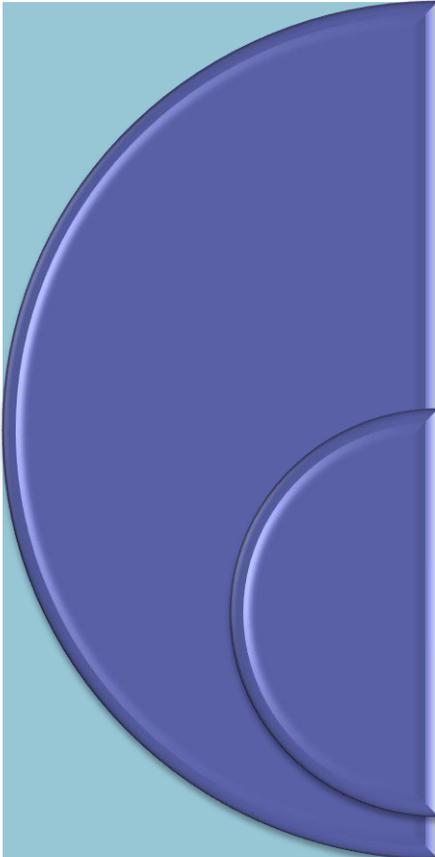
Since the 1930s, banks have not been allowed to pay interest on corporate checking accounts

This prohibition of interest on demand deposit accounts was enforced through Federal Reserve Regulation Q.

# Interest Bearing Demand Deposit Accounts



# Interest Bearing



The Dodd-Frank Wall Street Reform and Consumer Protection Act allows for the payment of interest on demand deposit accounts and went into effect July 21, 2011

This promises to be the biggest game changer in account analysis and will turn the review of account analysis statements from a chore that we had to struggle through into a mandatory function

# How will banks react

Like most changes in the banking world, one of the primary considerations on how banks deal with interest payments is technology

- The capability of their existing billing systems to pay interest on account analysis
- The capability of their core systems to pay interest
- Their ability to adopt new technology fast enough
- Their desire to attract corporate DDA balances

Banks will need to decide their business approach to Hard Interest as well

# Models Banks May Follow

1. Hard Interest on all balances; no earnings credit

• ***Out with the old & in with the new***

2. No Hard Interest; only earnings credit

• ***If it ain't broke, don't fix it***

3. Earnings credit on compensating balances; hard interest on the excess

• ***The best of both worlds***

# Basic Model Variables

- **Option 1: “Hard” interest only, pay customer with dollars**
  - Hard interest rates usually higher than earnings credits rates
  - Customers pay tax on hard interest
  - Customers can expense charges
- **Option 2: No change. “Soft” earnings credit only**
  - Earnings credit rates usually lower than hard interest rates
  - Reserve requirement *might* reduce effective rate
  - Customers do not pay tax on soft credit
  - Customers cannot expense charges offset by soft credit
- **Option 3: Hybrid combination of “Soft” credit and “Hard” interest**
  - Soft credits offset fees, hard interest earned on excess balances
  - Soft credit not taxable while hard interest is
  - Reserve requirement rate may be a factor
  - Charges offset by soft credit cannot be expensed

# Models Banks May Follow

Like everything in account analysis it all comes down to the math

- To evaluate the model that would best suit our companies, we need to take a holistic look at the way we manage cash and the way we pay our fees

This will allow us to guide and select our banking partners based on the interest programs that best meet our needs

# More Variables in the Hard Interest Mystery

Typical total analyzed charges

Typical hard charges

Earnings credit rate offered by the bank

Hard interest rate offered by the bank

Deficit premiums

Typical collected balances

Monthly concentration transfer fees

Funds availability schedule

Average daily float

Typical excess or deficit balance position

# Evaluating Your Interest Preference

Depending on your cash management strategies, cash flow profile and your strategy towards bank fees, you can effectively model the various interest possibilities

With this information in your hands, you will be able to shop for banking partners offering interest and service offerings that match your goals

What was once a consideration only of service price and quality just got a lot more interesting

# Relationship Based Pricing

Many banks now have the ability to evaluate your entire relationship with them

- You should review your overall portfolio with each bank as part of your fee negotiation strategy
- What credit facilities are in place with each bank?
- What investment activities do we use at each bank?
- Track this information as part of your account analysis

# Banks Under Pressure

Banks are under a great deal of pressure to recoup lost revenue sources and cover new costs

While this is understandable, we need to watch our account analysis closely and negotiate from strength

- Reasonable Service Pricing Comparable to other banks and customers
- Reasonable FDIC Fees Comparable to other banks
- Earnings Credit Rate pegged to a standard and Competitive
- Hard Interest Rate pegged to a standard and Competitive
- No Reserve Reduction
- Consider your Credit Facilities in your bank relationships
- How much of your wallet does each bank have?

# Treasury Under Pressure

## Interest on DDA's is available now

- Negotiate now while rates are low
- What do you mean the interest rate is negative?

## FDIC unlimited coverage for non-interest bearing accounts is available through 12/31/2012 and maybe beyond

- Bank Counterparty risk vs. Hard Interest

## Evaluate and Model your entire cash operation based on interest bearing DDA

- Can you leave more balances in DDA?
- Could you simplify your concentration schemes?
- Could you reduce or eliminate investment sweeps?
- Do you need controlled disbursement?
- At what rate does the ROI make sense?
- How do your credit facilities line up with your service providers?

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Thank You!  
Questions?

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# Additional Take Away Information

# Simplified Acct Analysis Stmt

## Balances

Average Ledger Balance	\$1,000,000.00
Less Average Float	\$50,000.00
Average Collected Balance	\$950,000.00
Average Negative Collected Balance	\$10,000.00
Average Positive Collected Balance	\$960,000.00
Less Federal Reserve requirement at 10%	\$96,000.00
Investable Balance	\$864,000.00
Multiplier	\$3,364.06
Less Balance Required	\$69,621,162.70
Excess / (Deficit) Collected Balance	-\$68,757,162.70

## Compensation

Earnings Credit Rate	0.3500%
Earnings Allowance	\$256.83
Less Ttl Analyzed Charges	\$20,695.61
Excess / (Deficit) Earnings Allowance	-\$20,438.77
Ttl Hard Charges	\$0.00
Net Fees Due	\$20,438.77
Ttl Service Charges	\$20,695.61

Service Description	AFP Code	Volume	Price	Total Fee	Required Balance
FDIC Insurance	00-0230	1,000	0.13%	110.41	371,428.57
Negative Collected Interest Assessment	00-0210	10,000	3.25%	27.60	92,857.14
Account Maintenance	01-0000	5	20.0000	100.00	336,405.53
Currency Deposited per \$1	10-0015	120,158	0.0009	108.14	363,796.34
Checks Deposited	10-022Z	81,000	0.0900	7,290.00	24,523,963.13
Controlled Disb Maintenance	15-0000	1	25.0000	25.00	84,101.38
Checks Paid	15-0110	2,500	0.1000	250.00	841,013.82
ACH Credits Received	25-0201	25	0.1200	3.00	10,092.17
ACH Debits Originated	25-0100	10	0.1200	1.20	4,036.87
Domestic Reporting Maintenance	40-001Z	5	50.0000	250.00	841,013.82
Domestic Reporting Transactions	40-023Z	83,535	0.1500	12,530.25	42,152,453.92
				<b>20,695.61</b>	<b>69,621,162.70</b>

# The Balance Required Multiplier

What is the multiplier?

The multiplier is the compensating balance required to offset \$1 of balance compensable service charges.

Example: I receive an earnings credit rate of 0.35%.

$$\$1 / (0.35\% \times (31/365)) = \$3,364.06$$

Earnings Credit Rates Adjusted for Reserves

Unadjust the ECR:  $\$1 / ((0.35\% \times (1+10\%)) \times (31/365))$

Adjust the ECR:  $\$1 / ((0.35\% \times (1-10\%)) \times (31/365))$

# Determine Your Bank's Handling of Reserves

If you really want to look into the EDI 822 to see if the ECR is adjusted for reserves.....

```
ISA*00#          *00#          *01#XXXXXXXXXX          *01#XXXXXXXXXX          *110705*162
5*U*00401*XXXXXXXXXX*0#P#!\GS*AA*XXXXXXXXXX*XXXXXXXXXX*20110705*9999*XXXXXXXXXX*X*004
010\ST*822*XXXXXXXXXX\BGN*00*XXXXXXXXXX*20110705*999999*ET\DTM*150*20110601\DTM*151*
20110630\DTM*009*20110705\N1*BK*CITYBANK, N.A.*13*999999999\N2*CASH MANAGEMENT\N
3*999 THE STREET\N4*NEW YORK*NY*10043*US\PER*IC*CONTACT NAME TE*5557771212\RT
E*1*.000\DTM*151*20110630\RTE*2*.250\DTM*151*20110630\RTE*4*.00000\DTM*151*20110
630\RTE*7*.13040\
```

Open the 822 in notepad and find RTE\*2. In the sample above the earnings credit rate is .25%. If there was an "A" after the 2 the earnings credit rate is 'Net of Reserves'. The other rates we are seeing are:

RTE\*1 reserve requirement .000

RTE\*4 collected balance overdraft interest rate .00000

RTE\*7 FDIC .13040

# Compensating Balances vs Fees Only

## Balances or Fees?

### Assumptions

Analyzed Charges (00-0331)	20,715.59
Earnings Credit Rate	0.2500%
Multiplier	4,709.68
Hard Interest Rate	0.0200%



### Compensating Balance Model

Balance Required	97,563,769.72
Plus cushion %	2.0000%
Total Balance required	99,515,045.11

### Fee Approach

	<u>Income</u>	<u>Expense</u>
Analyzed Charges (00-0331)		20,715.59
Hard Interest (30/360)	1,658.58	
Additional items		
<b>Net Income before tax</b>	<b>1,658.58</b>	<b>- 20,715.59 = (19,057.01)</b>
Less tax on Hard Interest at % 35%	-	
<b>Net gain (loss)</b>	<b>(19,057.01)</b>	

# Compensation Analyzer

## Assumptions

Earnings Credit Rate	0.2500%
Hard Interest Rate	0.5000%
Spread	0.2500%
Tax Rate	35.0000%

## Model A - Hard Interest Only

This model is based on the bank offering hard interest only on all net investable balances with no earnings credit offset

## Model B - Earnings Credit Only

This model is based on the bank offering earnings credit only on all net investable balances with no hard interest

## Model C - Earnings Credit & Hard Interest on Excess Balances

This model is based on the bank offering earnings credit on net investable balances up to the point where all balance compensable services have been covered and hard interest on any remaining net investable balances

Net Investable Balance	\$864,000.00	\$864,000.00	\$864,000.00
Total Balance Compensable	\$20,715.59	\$20,715.59	\$20,715.59
Approximate Earnings Credit	\$0.00	\$180.00	\$180.00
Total Balance Required	\$0.00	\$97,563,769.72	\$97,563,769.72
Excess/Deficit Investable Ba	\$0.00	(\$96,699,769.72)	(\$96,699,769.72)
Approximate Hard Interest P	\$360.00	\$0.00	\$0.00
Approximate Taxes Paid on	\$126.00	\$0.00	\$0.00
<b>Net Income</b>	<b>\$234.00</b>	<b>\$0.00</b>	<b>\$0.00</b>
<b>Net Expense</b>	<b>(\$20,715.59)</b>	<b>(\$20,715.59)</b>	<b>(\$20,715.59)</b>
<b>Net Profit / (Loss)</b>	<b>(\$20,481.59)</b>	<b>(\$20,715.59)</b>	<b>(\$20,715.59)</b>