Banking and Finance Law Daily Wrap Up, TOP STORY—OCC revises guidance on third-party relationships, (Oct. 31, 2013)

Banking and Finance Law Daily Wrap Up

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The Office of the Comptroller of the Currency has replaced its 2001 guidance on how national banks and federal thrifts should manage their relationships with third-party vendors. The OCC said that financial institutions are continuing to expand their use of third parties to perform many functions and added that it is concerned that the quality of risk management is not keeping up with this expansion. The agency put special emphasis on the need to manage the risks that arise from third-party relationships that involve an institution's critical functions (OCC 2013-29).

The guidance notes that banks face new or increased operational, compliance, reputation, strategic, and credit risks when engaging in third-party relationships. The OCC advises banks to adopt risk management processes commensurate with the level of risk and complexity of their third-party relationships, and expects more comprehensive oversight and management of third-party relationships that involve critical bank activities. To manage risks from third-party relationships, banks should:

- develop a plan that outlines the bank's strategy, identifies the inherent risks of the activity, and details how the bank will select, assess, and oversee the third party;
- perform proper due diligence to identify risks and select a third-party provider;
- negotiate written contracts that clearly outline the rights and responsibilities of all parties;
- conduct ongoing monitoring of the third party's activities and performance;
- execute a plan to terminate the relationship in a manner that allows the bank to transition the activities to another third party, bring the activities in-house, or discontinue the activities;
- assign clear roles and responsibilities for overseeing and managing third-party relationships and the risk management process;
- maintain proper documentation and reporting to facilitate oversight, accountability, monitoring, and risk management; and
- conduct independent reviews of the risk management process to enable management to assess that the bank's process aligns with its strategy and effectively manages risks from third-party relationships.

Third-party relationships include business arrangements between the bank and another entity, by contract or otherwise. The OCC cautions banks that use of third parties does not diminish the responsibility of the board and management to ensure the activity conforms to safe and sound banking practices and complies with applicable laws.

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