



SENT VIA ELECTRONIC MAIL

Ms. Ann E. Misback, Secretary
Board of Governors of the Federal Reserve
System
20th Street and Constitution Avenue NW
Washington, DC 20551

Chief Counsel's Office
Attention: Comment Processing
Office of the Comptroller of the Currency
400 7th Street SW, Suite 3E-218
Washington, DC 20219

James Sheesley, Assistant Executive Secretary
Attention: Comments – RIN 3064-ZA26
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

**Re: *Proposed Interagency Guidance on Third-Party Relationships: Risk Management*
Docket Numbers: FRB Docket No. OP-1752; OCC-2021-0011; FDIC RIN 3064-ZA26.**

The Innovative Lending Platform Association (ILPA) appreciates the opportunity to provide comments to the Board of Governors of the Federal Reserve System (FRB or Board), the Office of the Comptroller of the Currency (OCC), and the Federal Deposit Insurance Corporation (FDIC) (“the agencies”) regarding the *Proposed Interagency Guidance on Third-Party Relationships: Risk Management*.

ILPA members strongly support responsible financial innovation and believe that financial technology providers help augment business decision-making and risk management practices while enhancing services available to consumers and small business owners. Millions of small business banking customers currently depend on financial technology provided by ILPA members and will do so in the future. Continued innovation can benefit both financial institutions and their customers as well as serving as a mechanism for risk management, including the ability for financial institutions to assess risk internally and externally as well as combat fraud and cyber threats.

ILPA commends the efforts of the agencies to modernize and promote consistency in third-party risk management guidance and in practice. While championing the need for streamlined, clear, and timely regulatory guidance to be provided to financial institutions, ILPA members also believe the agencies need to proceed with care to ensure relevance and coherence alongside rapidly changing technology and significant regulatory developments. The proposal should ensure that the guidance does not hinder partnerships between insured depository institutions and third-party service providers but rather allow for the continued development of such relationships with clear guidelines for the benefit of small business borrowers.

About ILPA

ILPA is the leading trade organization for online financing and service companies serving small businesses. Our member companies¹ share a commitment to the health and success of our nation's small businesses and dedicate themselves to advancing best practices and standards that promote responsible innovation and access to capital. Our members have provided over \$50 billion to more than 1 million small businesses in a variety of industries, from restaurants to construction to hair salons and beyond. Our members provide financing from \$5,000 to \$500,000 with an average loan size of between \$35,000 and \$80,000, primarily to businesses with fewer than 10 employees.

As small business lending platforms, ILPA members have a tangible impact on our nation's businesses every day. ILPA members believe that in order to grow and invest in their business and employees, small business owners need access to timely and affordable credit. They need capital to purchase inventory and equipment, to upgrade or expand their facilities or operations, and to hire new workers. Unfortunately, small businesses have historically lacked access to capital, a challenge exacerbated by the Great Recession. The cost and approach of traditional underwriting practices continue to render "Main Street" lending not economically viable for many banks, resulting in a credit gap for small businesses that risks their success and vitality. ILPA members leverage innovative technologies, business models, and bank partnerships to fill that gap.

General Comments

While ILPA understands that the proposed guidance is directed toward insured depository institutions, it has significant consequences for the third-party service providers, which include ILPA members and their customers. As technology service providers to financial institutions, many ILPA members are indirectly subject to federal supervision through their banking partners, and most have operational similarities to insured depository institutions due to their financial institution relationships. As third-party service providers to financial institutions, they are also subject to vendor due diligence, required to be compliant with third-party risk management guidelines issued by regulatory agencies, are audited regularly by their bank partners, and are subject to myriad state laws and regulations.

ILPA commends the efforts of the agencies to modernize and promote consistency in third-party risk management guidance and in practice. The proposed interagency guidance offers some welcome notes, including that a bank may enter into a third-party relationship even if the third-party would not meet the bank's lending criteria (OCC 2020 FAQ #16). This clarification

¹ Members of ILPA include A10 Capital, BFS Capital/Nuula, Biz2Credit, BlueVine, Fundbox, Funding Circle, Kabbage/AMEX, Lendio, Mulligan Funding, OnDeck/Enova, Paynet/Equifax

that a third-party relationship is not the same as an extension of credit will allow for the continued development of new and better technology offered by emerging fintech providers.

ILPA also applauds the additional guides that have been released by the agencies, including the joint agency “*Conducting Due Diligence on Financial Technology Companies: A Guide for Community Banks*” and the Federal Reserve’s “*Community Bank Access to Innovation through Partnerships*” paper. These guides generally reflect the spirit of the *Proposed Interagency Guidance on Third-Party Relationships* and provide common-sense considerations for banking institutions seeking to innovate and partner with financial technology providers.

As the guidance notes, the financial services sector and especially the banking industry are using technology partners to remain competitive, provide compelling products and services to customers, and enhance overall operations. In seeking to further guide banking organizations and their third-party risk management, the agencies are attempting to provide and clarify certain risk-based principles on third-party risk management for institutions of all size. The guidance further describes the importance of a banking organization appropriately managing the risks of its third-party relationships, commensurate with their level of risk, and describes the need for more comprehensive and rigorous oversight and management of third-party relationships.

As part of this guidance, ILPA encourages the agencies to coordinate with the Consumer Financial Protection Board (CFPB) given its significant regulatory priorities will also impact third parties, notably Section 1033 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”). The development of open finance or “open-banking” as required by President Biden’s “Executive Order on Promoting Competition in the American Economy”² will give financial services customers the right to own their financial data. Open banking will substantially impact third parties as the number and usage of products and services that rely upon small business customers’ ability to authorize companies that have no business (or other) relationship with a financial institution access to their financial data has grown in recent years. This growth in authorized data has been accompanied by expansion in the number of use cases including small business loan underwriting.

The proposed interagency guidance again affirms that bank management should determine the risks associated with each third-party relationship and that risk management practices should be commensurate with the level of risk and complexity of the relationship. However, not all regulated financial institutions are equally resourced nor are all third-party fintech providers the same. Banks, especially those with assets less than \$1 billion in value, may not share the same technological capacity or compliance structures as larger national banks. This reality is why community banks often partner with established fintechs to offer new and innovative products that reach more consumers and small business borrowers. These partnerships increase competition and product choice to the benefit of all. One aspect of the guidance is that it

² [Exec. Order No. 14036](#) of July 9, 2021



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does not meaningfully differentiate between large national banks and those smaller financial institutions that often partner with fintechs and other third parties.

The agencies should also recognize that financial technology continues to evolve to better serve more customers, particularly those in underserved and underrepresented communities. ILPA believes that financial technology providers can and will offer more to financial institutions to assess risk internally and externally, combat fraud and cyber threats, while also offering new products and services in a post-pandemic economy.

Specific Comments:

The following answers are submitted to the ILPA-relevant questions included in the agencies' proposed guidance.

B: Scope

3. In what ways, if any, could the discussion of shared due diligence in the proposed guidance provide better clarity to banking organizations regarding third-party due diligence activities?

Supporting an innovative marketplace for all of the thousands of financial institutions in the United States is required for improved consumer and small business financial outcomes as well as a globally competitive U.S. financial system. The proposal should take care to ensure that the guidance does not hinder partnerships between insured depository institutions and third-party service providers but rather assure the continued development of such relationships with clear guidelines.

ILPA members often leverage a bank partnership model to help small businesses owners responsibly access capital in a timely manner. The bank partnership model between third-party providers and regulated financial institutions is based on a case-by-case situation. The focus of the guidance should take care to note that not all fintechs or financial institutions are the same. As such discretion in certain aspects of these relationships is absolutely paramount in minimizing arbitrary or burdensome barriers to innovate.

The agencies should note that the objective of this guidance must be to ultimately *increase* the number of technology firms that partner safely and securely with regulated financial institutions. If the guidance does not allow for more partnerships, competition as well as products and services currently offered by such arrangements will undoubtedly suffer. If a financial institution cannot reasonably assess if it can either afford to comply to agency standards when entering into a relationship with a financial technology provider, the guidance is more likely to harm smaller, less-resourced institutions and ultimately customers.



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For additional clarity, the Agencies should clarify that certain “typical” risk management practices are not suited for every situation – actions should be both relevant to the nature of the third-party relationship and warranted by the risks posed. The Agencies should establish a control framework to set reasonable risk management principles for each class of entity. This framework should be implemented to address the risk profile of each entity and set a reasonable industry standard approach,

C: Tailored Approach to Third-Party Risk Management

7. In what ways, if any, could the proposed guidance be revised to better address challenges a banking organization may face in negotiating some third-party contracts?

While appreciative that more specific guidance around third-party risk management is meant to provide clarity for fintech partners and lenders, ILPA has concerns regarding guidance in the area of third-party contracts. Many banks will interpret best practice guidance around third-party contracts as regulatory requirements. For example, a statement like “Generally, a third-party contract includes provisions for periodic, independent, internal, or external audits of third party, and relevant subcontractors” will be interpreted by many banks as a blanket requirement.

Since independent audits are expensive and not all third-party relationships warrant such an expense, the guidance needs to be very clear that contract negotiations with third parties, much like due diligence and other aspects of third-party risk management, must be approached on a case-by-case basis with the guiding principle being that the risk management practices (including contract negotiations) be commensurate with the level of risk and complexity of the third-party relationship.

ILPA believes the guidance around third-party contracts may extend beyond regulatory compliance risk-management and delve too far into what would normally be considered the province of legal rights/responsibilities negotiated between two contracting parties. Specifically, the guidance around “Cost and Compensation”, “Ownership and License”, “Indemnification”, “Insurance”, “Limits on Liability” and “Default and Termination” provide guidance regarding business decisions that should be freely negotiated between the contracting parties. Regulators need to understand that this “guidance” will be used by banks to strengthen their negotiating position at the cost and expense of third-party service providers which will ultimately reduce the number of third-party service providers willing or able to contract with banks and thereby harm small business customers.

D. Third-Party Relationships

10. What revisions to the proposed guidance, if any, would better assist banking organizations in assessing third-party risk as technologies evolve?

The agencies are all familiar with the challenge of trying to regulate rapidly changing technology without stifling innovation. It is critical that any new standards not be so inflexible that they quickly become outdated and become new unintentional roadblocks to innovation. These potential roadblocks, especially for smaller financial institutions and their customers, are what concerns ILPA members about the proposed guidance: in aggregate, the guidance suggests that third-party relationships could be a source of compliance and financial risk that outweighs any potential benefit of entering into the relationship. Again, the agencies should note that the objective of this guidance must be to ultimately *increase* the number of technology firms that partner safely and securely with regulated financial institutions.

11. What additional information, if any, could the proposed guidance provide to banking organizations in managing the risk associated with third-party platforms that directly engage with end customers?

ILPA members operate in a competitive environment and, as service providers, devote significant amounts of attention and resources to delivering the best experience possible for the end customer. Given the competition ILPA members face, they must continually ensure that the entire customer experience is streamlined and optimized. It should be noted here, as well, that direct customer feedback is a priority for ILPA members and is often a driver of improvements to customer experience.

Given this, ILPA believes any guidance related to third-party platforms that directly engage with end customers should provide the proper flexibility for third-party service providers to appropriately and efficiently update their platforms to respond to customer feedback and competitive forces in the marketplace.

Furthermore, the agencies may want to consider the inclusion of bright-line safe harbor provisions in the guidance that, if adhered to, would shield financial institutions from regulatory action. Safe harbor provisions allow for flexibility in third-party service arrangements since adherence to the provisions are not strictly required, while at the same time providing banks, particularly smaller institutions, with additional level of comfort in dealing with third parties in that they know if they satisfy certain safe harbor criteria, they are not opening themselves up to regulatory action by way of actions taken by third-parties.

G. Information Security

17. What additional information should the proposed guidance provide regarding a banking organization's assessment of a third party's information security and regarding information security risks involved with engaging a third party?

Even a perfectly designed third-party risk management framework will still see the potential for bad actors to access customer data, regardless of security controls. This truth is underscored by the fact that even the largest, most complex, and most highly regulated financial institutions have been victims of cybercrime in recent years. A key component of a well-regulated finance system is shared responsibility across the system, should an adverse event occur. Thus, assuring small business customers that, in the event they experience sustained harm because of an adverse event, the party responsible for the event will be held liable for making them whole, should be a foundational component of both the agencies' third-party supervisory expectations.

H. OCC's 2020 FAQs

18. To what extent should the concepts discussed in the OCC's 2020 FAQs be incorporated into the guidance? What would be the best way to incorporate the concepts?

ILPA notes that the OCC's 2020 FAQs provide third-party provider and regulated financial institutions more clarity regarding how such relationships should be considered and measured. While conducting reasonable due diligence of a third-party that conducts "critical activities", it is not the same as ensuring that the third-party would meet the lending criteria of that financial institution. This FAQ wisely separates prudent and reasonable due diligence from credit-based underwriting decisions which is not related to the goods or services offered by the third-party provider. The underlying logic in this rule will allow for the continued development of new and better technology offered by emerging fintech providers.



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Conclusion

ILPA appreciates that the agencies are trying to better enable all financial institutions, regardless of size, to partner with third-party service providers to competitively offer innovative products and services to their customers. To maximize market competition and consumer choice, financial institutions should be encouraged to partner with innovative third-party technology providers under clear supervisory guidelines. We appreciate the efforts of the regulators towards establishing a clear and consistent path for more such partnerships to the benefit of consumers and ILPA's small business customers.

Thank you for the opportunity to comment on this important guidance.

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