World Council

January 8, 2021

Submitted electronically

Randal K. Quarles
Chair
Financial Stability Board
Bank for International
Settlements CH-4002
Basel, Switzerland

Re: Outsourcing and third-party relationships

Dear Chairman Quarles:

World Council of Credit Unions (World Council) appreciates the opportunity to comment on the Discussion Paper regarding *Regulatory and Supervisory Issues Relating to Outsourcing and Third-Party Relationships.*[1] Credit unions are cooperative depository institutions and World Council is the leading trade association and development organization for the international credit union movement. Worldwide, there are over 85,000 credit unions in 118 countries with USD 2.1 trillion in total assets serving 274 million physical person members.[2]

World Council response to FSB's Questions for Consultation are below:

1. **What do you consider the key challenges in identifying, managing and mitigating the risks relating to outsourcing and third-party relationships, including risks in sub-contractors and the broader supply chain?**

Many credit unions utilize third parties to assist them in carrying out various functions of their operations. These relationships are often very beneficial and allow the credit union to perform tasks or obtain expertise that would not otherwise be unavailable to them. Credit unions as a whole are much smaller than their banking counterparts and often do not have the capital or resources available to larger banks. Their risks often arise from their lack of bargaining power due to their small size or perceived small volume of business and are often unable to negotiate favorable contractual clauses. These contractual risks often pose risk to the credit unions. They often are forced to accept these terms or forego the desired service.

We note that in the United States, the credit union prudential regulator, the National Credit

[1] Financial Stability Board, *Regulatory and Supervisory Issues Relating to Outsourcing and Third-Party Relationships*, November 9, 2020; available at https://www.fsb.org/wp-content/uploads/P091120.pdf.
[2] World Council of Credit Unions, *2018 Statistical Report* (2019), *available at* http://www.woccu.org/publications/statreport.

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Union Administration does not have authority to supervise third-party vendors or contractors.[3] However, they require contractual terms that require access to all books and records of any third-party vendor (*See* 12 C.F.R. § 712.3(d)(3)). Sometimes, due to the relative weak bargaining position of a credit union a vendor will not accept this term forcing a credit union to seek the services of an alternate vendor. This places an undue burden on the credit union and perhaps in the position of foregoing the services or forced unnecessarily into an alternate relationship that is more costly and less productive. We do note that the NCUA is seeking authority over third party vendors, however, we assert that their current authority is sufficient given the size and complexity of the institutions that they supervise.

The second challenge comes from the compliance burden often required from regulatory agencies during the process of performing due diligence or evaluations of third parties. Regulators often require much more than is necessary given the relationship or the services being provided. Often the regulatory burdens for due diligence are quite extensive and require a large amount of work and documentation. There should be an allowance to tailor the appropriate amount of due diligence based on a risk assessment.

2. What are possible ways to address these challenges and mitigate related risks? Are there any concerns with potential approaches that might increase risks, complexity or costs?

Proportional and risk-based regulation and supervision is the most effective way of regulating smaller institutions such as credit unions. Proportional guidelines and regulations that consider the size, risk and complexity of each entity will allow credit unions to implement and monitor risk without subjecting them to overburdensome regulations that are not applicable to the individual risk of that entity, and in effect strips resources and capital from the underserved banking community who benefit from the much needed services credit unions provide them. Augmenting compliance responsibility requires additional staff, training, and other resources many credit unions do not have.

Additionally, legal frameworks should level the playing field between small providers and large companies that will not and are not required to tailor unfavorable legal clauses that create risk for the credit unions. These often include limitations on liability, limitations on remedies, prohibition to access courts or other favorable dispute resolution mechanisms, evergreen clauses, exorbitant fees for additional services when problems arise, etc.

3. What are possible ways in which financial institutions, third-party service providers and supervisory authorities could collaborate to address these challenges on a cross-border basis?

Continued engagement of a diverse group of financial and non-financial institutions is imperative. In addition to the solicitation of public comments-- interactive webinars, focus groups and think tanks, and a task group charged with the responsibility researching and finding effective solutions could provide valuable insight and prescriptive collaboration that will

[3] *See* NCUA Office of Inspector General Report *Audit of the NCUA's Examination and Oversight Authority Over Credt Union Service Organizations and Vendors* (Report #OIG-20-07) September 1, 2020 *available at* https://www.oversight.gov/sites/default/files/oig-reports/ncuaoig-audit-cusos-vendors-2020.pdf.

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benefit all parties.

4. What lessons have been learned from the COVID-19 pandemic regarding managing and mitigating risks relating to outsourcing and third-party relationships, including risks arising in sub-contractors and the broader supply chain?

COVID-19 has presented numerous challenges for credit unions including the challenge of providing our members with access to remote financial services. The pandemic has created an urgency to make strides towards greater digital transformation, particularly for those financial institutions that still lack online and mobile transaction services. Health concerns brought on by the pandemic have led to a decline in branch visits and cash transactions for credit unions around the world. This trend is not likely to change once the pandemic subsides.

This need for digitization for credit unions will inherently mean the reliance on third party relationships to assist in the transformation. We do acknowledge that the volume and complexity of these relationships will continue to increase over time bringing with it increased risk, supply-chain risk, IT risk, privacy risks, reputational risks and others. They key, however, is understanding that the transformation is likely mandatory if a business or financial institution intends to survive as a viable entity. With that in mind, crafting regulations that balance the ability to have access to third party providers in an affordable manner so long as the proportional risks are managed adequately by the credit union is imperative.

World Council appreciates the opportunity to respond to the FSB's Discussion Paper on *Outsourcing and Third-party Relationships.* If you have questions about our comments, please feel free to contact me at pmonford@woccu.org or +1-202-510-9347.

Sincerely,

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Advocacy Counsel
World Council of Credit Unions