2017 RMA LARGE & REGIONAL BANKS ASSET SIZE: MORE THAN $50 BILLION THIRD-PARTY RISK MANAGEMENT SURVEY- EXECUTIVE SUMMARY

FINAL REPORT
OCTOBER 2017

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Operational Risk

ACKNOWLEDGMENTS

The 2017 survey was designed with the help of RMA's Vendor Risk Management Steering Committee, comprised of Debbie Manos-McHenry (Huntington Bank), John Klapmust (Bank of the West), Linda Quong (Charles Schwab), and Linda Tuck Chapman (ONTALA Performance Solutions Ltd).

The purpose of the survey was to capture the range of practices in third-party risk management over a cross section of RMA member institutions, and to gather detailed information on current and best practices and challenges in third-party risk management.

The final report provides participants' responses, while protecting the confidentiality of individual institutions by masking the source of the responses.

Note: Due to rounding, percentages in the tables may not add up to 100.

The RMA staff member contributing to the study was Sylwia M. Czajkowska.

Institutions (30) that participated in the survey:

Anonymous
Bank of the Ozarks
Bank of the West
BB&T
Bank of Montreal
BNY Mellon
Capital One
Charles Schwab & Co., Inc.
Citizens Bank
CoBank
Credit Agricole Corporate and Investment Bank
Discover Financial Services
First Republic Bank
HSBC
Huntington Bank
KeyBank
M&T Bank
Morgan Stanley
MUFG Union Bank
National Bank of Canada
PNC Bank
RBC

Regions Bank
Societe Generale
State Street Bank
Sun Life Financial
SunTrust Banks, Inc.
Toronto Dominion Bank Group
U.S. Bank
Zions Bank

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The Risk Management Association (RMA) is a not-for-profit, member-driven professional association serving the financial services industry. Its sole purpose is to advance the use of sound risk management principles in the financial services industry. RMA promotes an enterprise approach to risk management that focuses on credit risk, market risk, operational risk, securities lending, and regulatory issues. Founded in 1914, RMA was originally called the Robert Morris Associates, named after American patriot Robert Morris, a signer of the Declaration of Independence. Morris, the principal financier of the Revolutionary War, helped establish our country's banking system.

Today, RMA has approximately 2,500 institutional members. These include banks of all sizes as well as nonbank financial institutions. RMA is proud of the leadership role its member institutions take in the financial services industry. Relationship managers, credit officers, risk managers, and other financial services professionals in these organizations with responsibilities related to the risk management function represent these institutions within RMA. Known as RMA Associates, more than 18,000 of these individuals are located throughout North America and financial centers in Europe, Australia, and Asia.

Members actively participate in the RMA network of chapters. These chapters are run by RMA Associates on a volunteer basis and they provide our members with opportunities in their local communities for education, training, and networking throughout all stages of their financial services career. Chapters are located across the U.S. and Canada as well as in global financial centers.

RMA members also avail themselves of benefits offered through headquarters in Philadelphia, Pennsylvania. To assist members in advancing sound risk management principles, RMA keeps members informed and provides access to industry information at this site; publishes *The RMA Journal* and a variety of newsletters, books, and statistics; conducts workshops and seminars; holds conferences, including an annual convention (Annual Risk Management Conference); and has numerous committees working on a variety of projects.

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Note: As a not-for-profit, professional association, RMA does not lobby on behalf of the industry.

EXECUTIVE SUMMARY

The survey was conducted by The Risk Management Association (RMA) between June and August 2017. Most of the questions were multiple choice with opportunities to provide comments. Some questions were open text, designed to provide information and insight about best and current practices.

A total of 30 responses from large and regional size banks were received, covering a range of asset sizes over $50 billion. This year, RMA decided to conduct separate surveys for mid-tier banks, large and regional banks, and community banks.

Participating institutions were asked to provide their primary regulator for context and further analysis. As expected, all participating institutions are regulated by one or more of the following: OCC, FRB, and FDIC.

The following areas were addressed in the survey:

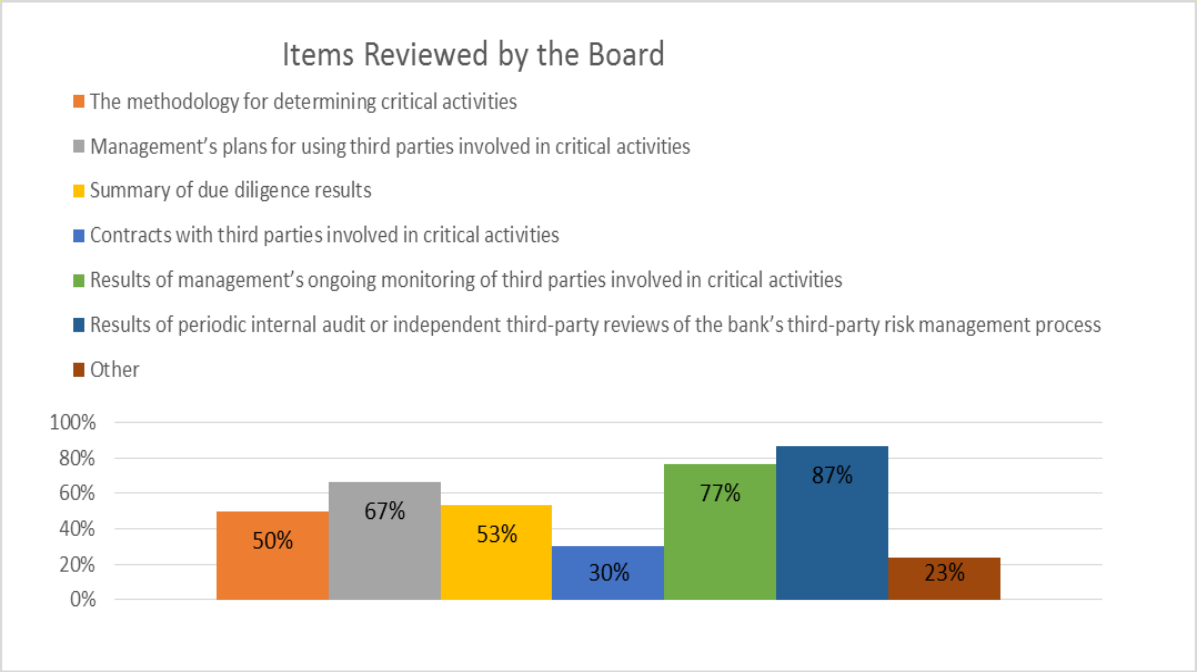
1. Third-Party Risk Management Framework.
2. Third-Party Selection and Monitoring Process.
3. Critical Third-Parties and Critical Activities.
4. Tools and Technology.
5. Contracts.
6. Regulatory and Compliance.
7. Fourth Parties.

Some questions were repeated from the 2014 and 2015 baseline surveys. This will help financial services companies track their progress and evolution of practices.

Third-Party Risk Management Framework

When asked about the Board of Directors' involvement with third-party risk management, a majority of institutions (>80%) confirmed that their Board ensures that strategies related to the bank's core competencies appropriately address which services to retain and which services to outsource to third parties. Key items reviewed by the Board include (in the order of highest responses):

- Results of periodic internal audit or independent third-party reviews of the bank's third-party risk management process.
- Results of management's ongoing monitoring of third parties involved in critical activities.
- Management's plans for using third parties involved in critical activities.
- Summary of due diligence reports.
- The methodology for determining critical activities.



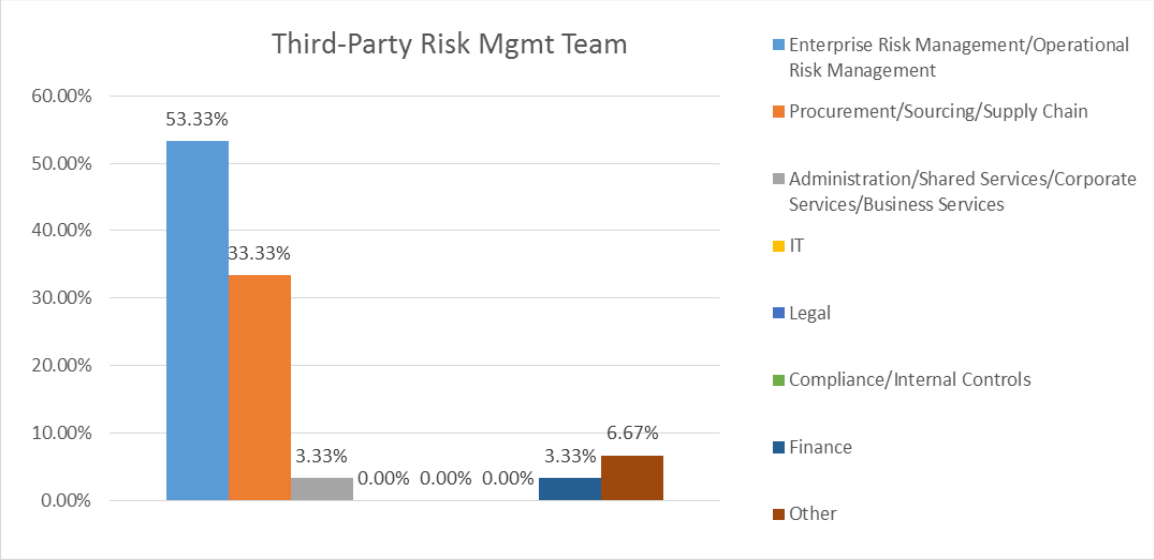
For 80% of respondents, the institution's overall strategy for third-party risk is well understood and fully aligned with the institution's overall risk appetite.

Third-party risk management programs are evolving quickly. In the 2014 survey, 0% of respondents described their "vendor" third-party risk management program as fully mature. In the 2015 survey, almost 30% indicated that their program is fully mature and 26% of participating institutions reported that their program will be fully mature in less than a year. In this year's data, we see that 27% of participants consider their third-party risk management program to be fully mature and 53% will become fully mature in less than a year.

Response	**2017**	**2015**		**2014**	
Fully mature	26.67%	29.63%		1-Completely mature	0%
Will be fully mature in less than a year	53.33%	25.93%		2	25.8%
Doesn't address the full lifecycle yet	10%	29.63%		3	58.1%
New or underway	10%	14.81%		4	12.9%
				5-Not Mature at all	3.2%

Since 2014, there has been a shift in how the vendors are managed. About 53% of vendors are managed in the business, compared to 77% in the 2014 survey for the same asset size category.

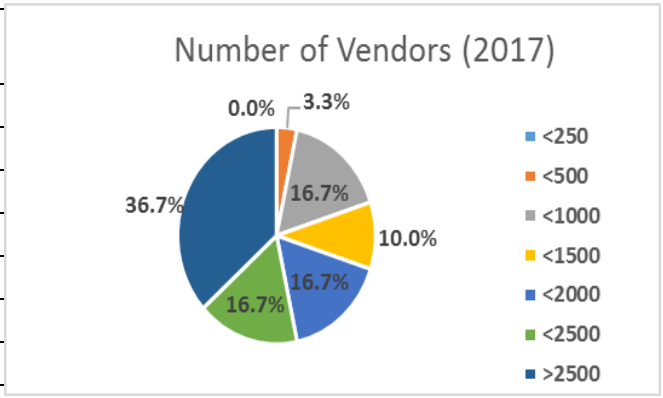
Similarly, as in the 2015 report, the team responsible for design, framework, policy/standards, and processes for third parties is primarily located in the Enterprise Risk Management/Operational Risk Management function.



The oversight function resides in the 2nd Line of Defense and is part of the same risk oversight area.

The composition of the number of vendors within the scope of the program has shifted since our last survey. About 33% of respondents predict that the current number of third parties will increase in the next two to three years and 43% predict that the number of vendors in their program will remain at the same level.

# of Vendors	2017	2015	2014
<250	0.0%	7.4%	16.1%
<500	3.3%	7.4%	16.1%
<1,000	16.7%	22.2%	9.7%
<1,500	10.0%	7.4%	3.2%
<2,000	16.7%	3.7%	3.2%
<2,500	16.7%	22.2%	3.2%
>2,500	36.7%	29.6%	48.4%



For institutions with asset size over $50 billion, the number of FTEs supporting related activities has changed from the 2015 survey.

Total # of FTEs	FTEs dedicated to:		
	"vendor" third-parties (2017)	"vendor" third-parties (2015)	"non-vendor" third-parties (2015)
<3	10%	11.11%	55.56%
3-5	10%	18.52%	11.11%
6-10	16.67%	18.52%	22.22%
11-15	23.33%	3.7%	3.7%
16-25	6.67%	7.41%	0%
>25	33.33%	40.74%	7.41%

Third-Party Selection and Monitoring

The main factor driving the process to identify the third parties that will be actively managed within an institution's third-party risk management program is determined by a risk profile calculator/algorithm built into the third-party risk assessment questionnaire (80% of responses). This is consistent with the 2015 report.

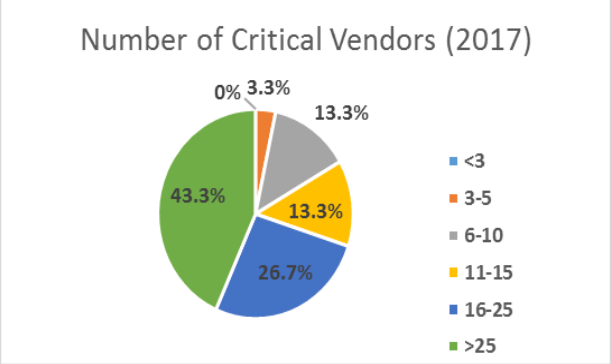
About 93% of the participants indicated they send due diligence questionnaires for risk assessment purposes, in addition to the RFP questions. The preferred alternatives to these questionnaires include: SOC (Types 1, 2, and 3), SSAE16 (Types 1 and 2) reports, National Institute of Standards and Technology, and ISO27001 certification.

Taking into consideration the amount of work required to review a vendor, 76% of respondents would be willing to consider using a shared assessment provided by a third party.

Critical Third Parties and Critical Activities

Over the years, the number of "enterprise critical" third parties has changed. Consistently, the figures show that the majority of institutions have more than 25 critical vendors or between 16 and 25 "enterprise critical" vendors—vendors that have the potential to bring the bank to its knees—in their programs.

# of Critical Vendors	2017	2015	2014
<3	0%	0%	3.2%
3-5	3.3%	3.7%	3.2%
6-10	13.3%	18.5%	6.5%
11-15	13.3%	7.4%	16.1%
16-25	26.7%	33.3%	12.9%
>25	43.3%	37.0%	58.1%



About 90% of respondents conduct site visits for their most and/or high risk critical third parties, while 29% of those who conduct site visits do so on an annual basis. Out of the 90% who conduct site visits, about 48% do not have resources dedicated to this task.

There is evidence that institutions are gaining clarity around third-party management requirements. For example, definitions of "critical activities" provided in the 2014 report were somewhat vague. The definitions are much more precise in this year's report. Furthermore, the definition of "critical activity" is fully defined for 69% of the institutions who contributed to the study. The remaining 31% are in the process of defining it.

The data also shows an upward trend related to requiring an exit strategy for critical supplier, likely in response to FFIEC's Appendix J on business continuity management. For years 2014, 2015, and 2017, the percentage of institutions requiring exit strategies was 67%, 89%, and 97%, respectively.

Workload management is a serious concern for third-party risk management professionals. For example, in response to the question, "Have you granted any blanket exceptions to specific categories of relationships/activities whereby they are exempt from due diligence that would otherwise be mandatory? (e.g., shrink-wrap software, appraisers, law firms, and government or quasi-government agencies)" (question 36), over 57% of survey participants responded positively and shared some of their practices.

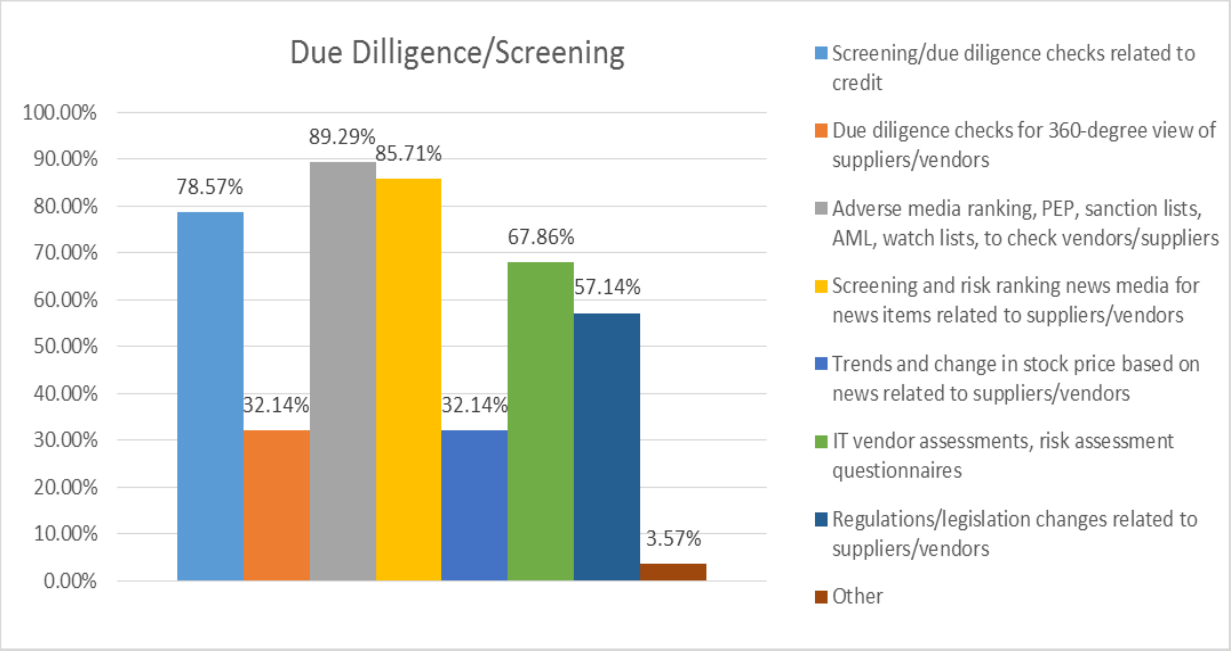
Tools and Technology

Technology adoption varies across institutions. Archer is a preferable third-party solution provider used by large and regional banks (67%). Some other commonly used programs include: Ariba, and Hiperos. In the 2015 survey, Archer was also selected as a top primary technology used for this asset size sector. We have noticed a spike in supplementing use of commercial providers with using MS Office programs and homegrown programs. In the 2015 survey, only 7.4% of participating institutions were using MS Access, Excel, or SharePoint to manage their third-party risk management programs, with higher numbers in smaller institutions. In 2017, that number increased to over 33%. When asked if institutions use the same primary technology to manage activities, documentation, and reporting for non-vendor third-party risk management programs, 56% of respondents selected "Yes." About 27% of institutions selected "Hybrid" and provided an explanation for doing so.

Most institutions acquire data from third parties like Dunn and Bradstreet, LexisNexis, Rapid Ratings, and Standard & Poor's to support due diligence and monitoring activities. The use of automated data feeds, automated alerts, and independent due diligence is an emerging practice, and most of the data comes from sources such as Dunn and Bradstreet and LexisNexis.

The most common types of due diligence that institutions use and/or are interested in obtaining are (1) adverse media ranking/PEP/sanction lists/AML/watch lists, (2) screening and risk rating for relevant news media for news items related to vendors/suppliers, (3)

screening/due diligence checks related to credit, and (4) IT vendor assessments/risk assessment questionnaires.



About 57% of respondents require cyber liability insurance from third parties that have access to personal and private information.

Contracts

About 80% of institutions use standard contract and risk control clauses for third-party relationships. This number is similar to year 2015 where 81% of respondents indicated they've implemented these standards. Standard contracts for vendors in 2014 were used by 19% of respondents.

Internal audit (93%), followed by ERM/ORM (43%), continues to play a key role in terms of conducting independent reviews of a third-party risk management program.

When it comes to the "Supplier Code of Conduct," 38% of respondents still do not have one in place. This is down from the 48% threshold noted in the 2014 data.

Once the contract is executed, 60% of institutions reassess risks for higher risk third parties on an annual basis. This number decreased from 74% in 2014. About 40% of this year's respondents indicated that this activity varies and is dependent upon one of the following: risk rating of the vendor, material changes, and regulatory requirements.

When asked about managing and reporting on third-party risk incidents and issues, consistently across the years, the top three responses were (in order from highest to lowest):

1. Reports risk incidents and issues to the company's operational and management committees.
2. Escalates risk incidents and issues to the business line, the company's risk subject matter experts, and upper management.
3. Regularly reports status of risk incidents and issues to the business.

We asked our members about outsourcing. Currently, 57% of institutions do not outsource any part of sourcing, procurement, or supplier risk management. Also 57% answered that none of their due diligence assessments have been outsourced to third-party providers.

Regulatory and Compliance

In most cases, the regulatory liaison (37%) or Enterprise/Operational Risk Management (23%) are responsible for identifying, tracking, and communicating regulatory and compliance updates/changes related to third-party risk management.

Approximately 80% of institutions have a risk oversight committee, formed specifically to oversee third-party risks. This is an increase from 70% noted in 2015.

The following information about regulatory criticism can be used as a guide for program evolution across the sector. Please refer to question 58 for additional information.

Response	Percent
Completeness: program doesn't address full lifecycle of "vendor" third-party relationships	27.27%
Completeness: program doesn't include all critical "non-vendor" third-party relationships and activities	22.73%
Consistency: program is not applied consistently across all lines of business	31.82%
Due diligence: quality and completeness, documentation	27.27%
Business continuity/resilience (new Appendix J to FFIEC guidance)	27.27%
Governance and oversight	45.45%
Controls	18.18%
Effective Challenge	22.73%
Monitoring	36.36%
Reporting	45.45%
Cybersecurity (e.g., horizontal Fed/OCC cyber review)	13.64%
Other (please specify)	31.82%

Fourth Parties

The final section of the survey was dedicated to fourth parties. There is a range of practices when it comes to how **material** fourth parties are identified.

- 14% require their third party to identify fourth parties during RFP process.
- 14% indicated that material fourth parties are identified in the contract.
- 21% require their third party to update the list of material fourth parties annually.
- 52% selected "Other" and provided their processes for identifying material fourth parties.

In 2014, 23% of those surveyed confirmed that they perform due diligence on fourth parties. That number is consistent with our 2017 data. It is worth mentioning that this year participants could select "Partially," in addition to "Yes/No" choices.

Insights

Please see the following pages for detailed responses and examples of the range of practices institutions with asset sizes over $50 billion employ for third-party/vendor risk management.

Thank you to RMA member banks for contributing to this benchmarking study. The full report is available to those institutions that contributed to the study.