Prepared for: Federal Deposit Insurance Corporation

Re: Request for Information on Standard Setting and Voluntary Certification for Models and Third-Party Providers of Technology and Other Services

RIN 3064-ZA18

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General

Question 1: Are there currently operational, economic, marketplace, technological, regulatory, supervisory, or other factors that inhibit the adoption of technological innovations, or on-boarding of third parties that provide technology and other services, by insured depository institutions (IDIs), particularly by community banks?

Answer: We have seen some challenges arise from the current global pandemic. Financial Institutions have had to adapt to a virtual environment, and their IT teams have been strained. Implementing new software, technology or tools while being faced with these challenges has had an impact. The economical impact has also strained budgets as they prepare for a possible downturn.

Question 2: What are the advantages and disadvantages of establishing standard- setting and voluntary certification processes for either models or third-party providers?

Answer: Our interpretation is that the FDIC's Voluntary Certification program would help to simplify one portion of the third party regulatory Model Validation Guidance process. The FDIC certifies that the software is working properly as designed, such as scenarios and government watch list scanning.

The other portions of the process that the FDIC certification wouldn't address is regarding the bank's data and the use of the software in a specific bank setting.

The performance of a model depends on the quality of the data being imported. If the bank's data is deficient it can possibly cause the model to not function as intended.

The FDIC Voluntary Certification process also doesn't assess if the model is calibrated specifically according to a bank's Risk Assessment.

Therefore the FDIC's Voluntary Certification process would help to ease part of the burden bank's face in adhering to regulatory Model Validation Guidance but not all. Banks would have to continue to engage third party auditors to assess significant portions of the current process.

Question 3: What are the advantages and disadvantages to providers of models of participating in the standard-setting and voluntary certification process? What are the advantages and disadvantages to providers of technology and other services that support the IDI's financial and banking activities of participating in the standard-setting and voluntary certification process?

Answer: The obvious primary advantage is that the FDIC would be familiar with the vendor and the model that underwent the certification process. This process would undoubtedly result in extensive and detailed documentation that would be shared with the field examiners for their reference when examining an institution with that model. Ideally, this concept could result in less time spent during the examination as the examiner could rely on the documentation and then directly target their questions to how the institution has customized the model and is using it based on their risk profile.

The most significant disadvantage is if the third-party and model don't pass or succeed in the certification process; how would this information be disseminated? Would the field staff be told that xyz company's model failed the process? If so, that could have significant consequences for the vendor's business but also for the banks that have already subscribed to and deployed that particular model. Would they be permitted to continue to use the model? Would their CAMELS rating be affected?

Question 4: What are the advantages and disadvantages to an IDI, particularly a community bank, of participating in the standard-setting and voluntary certification process?

No response provided

Question 5: Are there specific challenges related to an IDI's relationships with third-party providers of models or providers of technology and other services that could be addressed through standard-setting and voluntary certification processes for such third parties?

Answer: Maintaining an adequate vendor management process can be a time consuming demand, especially on the resources of a smaller community bank. If the voluntary certification process could remove the burden of gathering and analyzing a vendor or third-party's financial statements it would be a win for those financial institutions.

1) Are there specific challenges related to due diligence and ongoing monitoring of such third-party providers?

No Response Provided

2) Are there specific challenges related to the review and validation of models provided by such third parties?

The challenges to the community bank market, especially in the BSA area, is that there are several outside audits and examinations that the staff must prepare for and spend time facilitating during the year. There is the required annual independent BSA audit and regulatory examination. The bank may also undergo a voluntary outside engagement such as a Program Review or Efficiency and a Data Validation. In addition there is the Model Validation which is part of the regulatory guidance. The time spent preparing for, facilitating the process, and then responding to any findings is significant.

3) Are there specific challenges related to information sharing or data protection?

No Response Provided

Question 6: Would a voluntary certification process for certain model technologies or third-party providers of technology and other services meaningfully reduce the cost of due diligence and on-boarding for: (1) the certified third-party provider? (2) the certified technology? (3) potential IDI technology users, particularly community banks?

Answer: Costs to the community banks would be reduced if there was a voluntary certification process because the staff that would normally be charged with the responsibility of evaluating the new relationship with a potential third-parties could be working on other projects. In addition, the due diligence phase of the workings of the model could be reduced because the model has already been certified. The community bank could focus on whether or not that model accomplishes what they specifically need it to do.

Question 7: What are the challenges, costs, and benefits of a voluntary certification program or other standardized approach to due diligence for third-party providers of technology and other services? How should the costs of operating the SSO and any associated COs be allocated (e.g., member fees for SSO participation, certification fees)?

Answer: The challenge to implementing such a program we believe would be significant for the FDIC and especially during this time frame as the country's health and economic crisis may very well be transitioning into a banking crisis as well. Would this be done with the agency's IT Staff? or outsourced to a third party? Costs could be shared by those vendors who wish to participate.

Question 8: Would a voluntary certification process undermine innovation by effectively limiting an IDI's discretion regarding models or third-party providers of technology and other services, even if the use of certified third parties or models was not required? Would IDIs feel constrained to enter into relationships for the provision of models or services with only those third parties that are certified, even if the IDIs retained the flexibility to use third parties or models that were not certified?

Answer: Certainly some conservative institutions will want to play it safe and only engage with "certified" vendors and models. However, the industry will continue to evolve despite having this process or not.

Question 9: What supervisory changes in the process of examining IDIs for safety and soundness or consumer protection would be necessary to encourage or facilitate the development of a certification program for models or third-party providers and an IDI's use of such a program? Are there alternative approaches that would encourage or facilitate IDIs to use such programs?

Answer: It is our belief that the examination process should neither encourage or discourage the use of the certification program. There are various reasons that a vendor or third-party may or may not choose to become involved in the certification process and that should remain their option.

The FDIC can encourage the use of the certification program directly with vendors. They are aware of the various models that IDIs use so they can reach out.

Question 10: What other supervisory, regulatory, or outreach efforts could the FDIC undertake to support the financial services industry's development and usage of a standardized approach to the assessment of models or the due diligence of third-party providers of technology and other services?

Answer: Once the country returns to live events safely the FDIC can use industry conferences to meet with vendors as well as onsite visits to their offices and development centers.

When more specifics are known about the program the FDIC conduct webinars and carve an area on the FDIC's website for this program along with printed information and Q&A's.

Scope

Question 11: For which types of models, if any, should standards be established and a voluntary certification process be developed? For example, is the greatest interest or need with respect to: (1) traditional quantitative models? (2) anti-money laundering (AML) transaction monitoring models? (3) customer service models? (4) business development models? (5) underwriting models? (6) fraud models? (7) other models? or need with respect to: (1) traditional quantitative models? (2) anti-money laundering (AML) transaction monitoring models? (3) customer service models? (4) business development models? (5) underwriting models? (6) fraud models? (7) other models?

Answer: The voluntary certification process at first glance appears to lend itself well to anti-money laundering/transaction monitoring models very well. Also on the lending side the ALLL/ACL process along with stress testing would benefit from a certification process.

Question 12: Which technical and operational aspects of a model would be most appropriate for evaluation in a voluntary certification program?

Answer: For anti-money laundering, the model's scenario logic as well as the population and filing of SARs and CTRs.

For ALLL/ACL the technical calculations of the particular method chosen, such as Cohort or PD/LGD.

For stress testing, the calculations around the loss driver as well as the calculations on the impact to earnings and the IDIs capital basis.

Reporting capabilities of all three areas mentioned above would also be appropriate.

Question 13: What are the potential challenges or benefits to a voluntary certification program with respect to models that rely on artificial intelligence, machine learning, or big data processing?

Answer: There may be greater challenges for supervised AI/Machine Learning models because the data inputs may be proprietary rendering the process more difficult. There shouldn't be any extra difficulties with unsupervised models.

Question 14: How can the FDIC identify those types of technology or other services, or those aspects of the third-party provider's condition, that are best suited for a voluntary certification program or other standardized approach to due diligence? For example, should such a certification program include an assessment of financial condition, cyber security, operational resilience, or some other aspect of a third-party provider?

Answer: By using the FDIC's expertise in the areas of financial analysis, cybersecurity, and operational risk management.

SSO

Question 15: If the FDIC partnered with an SSO to set standards for due diligence and assessments of models or third-party providers of technology and

other services, what considerations should be made in choosing the SSO? What benefits or challenges would the introduction of an SSO into the standard-setting process provide to IDIs, third- party providers, or consumers?

No Response Provided

Question 16: To what extent would a standards-based approach for models or third-party providers of technology and other services be effective in an environment with rapidly developing technology systems, products, and platforms, especially given the potential need to reassess and reevaluate such systems, products, and platforms as technologies or circumstances change?

No Response Provided

Question 17: What current or draft industry standards or frameworks could serve as a basis for a standard-setting and voluntary certification program? What are the advantages and disadvantages of such standards or frameworks? Do standards and voluntary certifications already exist for use as described herein?

No Response Provided

Question 18: Given that adherence to SSO standards would be voluntary for third parties and for IDIs, what is the likelihood that third-party providers of models or services would acknowledge, support, and cooperate with an SSO in developing the standards necessary for the program? What challenges would hinder participation in that process? What method or approaches could be used to address those challenges?

No Response Provided

Question 19: What is the best way to structure an SSO (e.g., board, management, membership)? Alternatively, are there currently established SSOs with the expertise to set standards for models and third parties as described herein?

No response Provided

Question 20: To what extent should the FDIC and other federal/state regulators play a role, if any, in an SSO? Should the FDIC and other federal/state regulators

provide recommendations to an SSO? Should the FDIC and other federal/state regulators provide oversight of an SSO, or should another entity provide such oversight?

No Response Provided

Certification Organizations (COs)

Question 21: What benefits and risks would COs provide to IDIs, third parties, and consumers?

No Response Provided

2. Question 22: To what extent would COs be effective in assessing compliance with applicable standards in an environment with rapidly developing technology systems, products, and platforms, especially given the potential need to reassess and reevaluate such systems, products, and platforms as technologies or circumstances change?

No Response Provided

Question 23: For model validation and testing, would COs evaluate a model based solely on reports, testing results, and other data provided by the third-party provider of the model? Or would the COs need to test the model and generate their own test results? What steps would the COs need to take to protect the intellectual property or other sensitive business data of the third party that has submitted its model to the validation process?

Answer: To provide the maximum value, the model's should be thoroughly tested to generate unique results. Models will have intellectual property appropriate non-disclosures or other legal arrangements should be made in advance.

Question 24: If COs receives derogatory information indicating that a certified third party or certified model or technology no longer meets applicable standards, should the COs develop a process for withdrawing a certification or reassessing the certification? (1) If so, what appeal rights should be available to the affected third party? (2) What notification requirements should COs have for financial institutions that have relied on a certification that was

subsequently withdrawn? (3) Should the FDIC or federal/state regulators enter information sharing agreements with COs to ensure that any derogatory information related to a certified third party or certified model or technology is appropriately shared with the COs?

Answer: The certifications should be issued for a certain length of time, possibly 12 or 24 months. At the time of maturity then a re-certification process can be performed. During the interim we don't believe there should be any formal supervisory authority or action that can be taken by the FDIC. If derogatory information is received by the agency there could possibly be an informal process or inquiry undertaken but this should stop short of becoming supervisory action.

5. Question 25: Are there legal impediments, including issues related to liability or indemnification, to the implementation of a voluntary certification program that the FDIC, other federal/state regulators, third-party providers, and IDIs should consider?

No Response Provided

6. Question 26: To what extent should the FDIC and other federal/state regulators play a role, if any, in the identification and oversight of COs, including assessments of ongoing operations? Should the FDIC and other federal/state regulators provide oversight of COs, or should another entity, such as an SSO, provide such oversight?

Answer: There should be an evaluation during the certification and re-certification process but the new program should not result in an regulated industry as these are private companies that are not funded with insured deposits.