



IOWA DIVISION OF BANKING

EXPLORING A FINTECH? ITEMS FOR CONSIDERATION

Overview

Innovation and technology are transforming the financial services landscape. As the banking industry becomes more complex and technologically driven, financial technology (fintech) is being brought to the forefront. Fintech companies offer possible partnerships and collaborative relationships for community banks as they work to respond to the evolving needs of the market.

Assessing and controlling the risks posed by a potential fintech relationship is key to ensuring the activity is conducted in a safe and sound manner. Numerous risks may arise from the use of a third-party and some risks may be associated with the underlying activity itself.

This resource provides items for banks to consider when exploring relationships with fintech companies, however, it is not intended to be all-encompassing. Community banks should ensure alignment with the strategic and business objectives of the bank, and maintain adequate systems to identify, measure, monitor, and control all risks associated with the fintech activity.

Due Diligence

An effective third-party risk management program includes due diligence as an important component. The Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency collaborated to create a guide to assist community banks in conducting due diligence when considering relationships with fintech companies. In August 2021, the three federal banking agencies issued *Conducting Due Diligence on Financial Technology Companies – A Guide for Community Banks*. A link to a copy of the guide can be found under "Resources".

The guide identifies six key due diligence topics including:

- Business Experience and Qualifications
- Financial Condition
- Legal and Regulatory Compliance
- Risk Management and Controls
- Information Security
- Operation Resilience

Relevant considerations, potential sources of information, and illustrative examples are also included for each topic within the guide.

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Key Considerations

Before a community bank implements a new or innovative activity, it is important to identify and mitigate the associated risks. It is essential that the board and management establish appropriate policies, procedures, internal controls, and management information systems to effectively oversee the activity and ensure adherence to applicable laws and regulations. In addition to those items, consideration should be given to the following:

- **Management:** Establish a solid framework around the prospective activity. Dedicate sufficient resources and staffing to this activity, and make sure appropriate training is provided. Provide proper oversight, governance, and ongoing monitoring of the activity. Ensure an independent review or audit is conducted by a qualified auditor as part of the ongoing monitoring process.
- **Capital:** Plan for the potential impacts that the fintech activity can have on capital of the bank. Create robust monitoring practices to ensure maintenance of appropriate capital levels relative to the risk exposures posed by the activity.
- **Liquidity:** Integrate potential implications into the liquidity risk management function of the bank.
- **Earnings:** Establish a process to evaluate and monitor the adequacy of earnings performance from the fintech activity.
- **Sensitivity to Market Risk:** Incorporate the fintech activity into the interest rate risk model if applicable and ensure assumptions for the activity are appropriate.
- **Bank Secrecy Act/Anti-Money Laundering (BSA/AML):** Integrate the fintech activity into the BSA/AML framework.
- **Information Technology:** Ensure alignment with information security, controls, incident response, operational resiliency, and cybersecurity.

Community banks should give consideration to the information outlined in this resource when exploring relationships with fintech companies. Iowa state chartered banks may also need to obtain Superintendent approval under new Iowa Code section 524.802A before embarking on a new or innovative electronic activity. Details of Iowa Code section 524.802A can be found on the following page. For further information or questions, please contact a Bank Analyst at the Iowa Division of Banking by calling 515-281-4014.

Resources

- **Conducting Due Diligence on Financial Technology Companies – A Guide for Community Banks**
 - <https://www.fdic.gov/news/press-releases/2021/pr21075a.pdf>
 - <https://www.federalreserve.gov/publications/files/conducting-due-diligence-on-financial-technology-firms-202108.pdf>
- **Community Bank Access to Innovation through Partnerships**
 - <https://www.federalreserve.gov/publications/files/community-bank-access-to-innovation-through-partnerships-202109.pdf>

EXPLORING A FINTECH?

524.802A Electronic Activities of a State Bank

1. A state bank may conduct in electronic form any activities that are expressly authorized for state banks under any provision of this chapter, including in sections 524.801, 524.802, and 524.804, and activities that are the functional equivalent of any activities expressly authorized for state banks under this chapter. A state bank may perform, provide, or deliver through electronic means any activity, function, product, or service it is authorized to perform by any provision of this chapter and must comply with all applicable laws and regulations.

2. Subject to the prior approval of the superintendent, a state bank may, beginning on July 1, 2021, engage in new or innovative electronic activities that are part of the business of banking. When determining whether a state bank is authorized to engage in a new or innovative electronic activity that is not traditionally offered by banks via electronic means, the superintendent shall consider whether the activity is expressly authorized for state banks under this chapter, whether the activity is the functional equivalent of any activity authorized for state banks, whether the activity is a logical extension of any activity authorized for state banks, whether the state bank has the expertise necessary to understand and manage the activity, and whether the activity presents risks similar to those state banks already assume.

3. A state bank that engages in any new or innovative Senate File 586, p. 43 electronic activities must conduct these activities in a safe and sound manner and must maintain adequate systems to identify, measure, monitor, and control the risks associated with its electronic activities. These systems must include policies, procedures, internal controls, and management information systems governing the electronic activities of the state bank and may be tailored to the specific risks presented by the electronic activities of the state bank. A state bank engaging in new or innovative electronic activities must also maintain adequate and effective information security infrastructure and controls.

4. The superintendent may adopt rules pursuant to chapter 17A to implement the provisions of this section, including but not limited to application procedures, identifying the systems, processes, and technologies a state bank must maintain in order to engage in certain new or innovative electronic activities, and determining that additional new or innovative electronic activities are authorized for state banks without prior approval.