

Banking

Traditions

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BUSINESS CONTINUITY DURING A PANDEMIC

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- Community Banks' Leading Role in a Sustainable Future
- SOUTHERN HOSPITALITY MEANS BUSINESS!
- Increased Exposure in the New Cyber Era
- SUCCESSION PLANNING IS A MUST

Securing Your Bank's Future in Insecure Times

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PRICING ISSUES

Customers and vendors are likely to have many competing interests during contract negotiations. While a customer wants to obtain a reasonable price, a vendor needs to be able to sell its product or service at a price sufficient to generate a profit. In order to attract customers in down economic times, vendors will often offer reduced fees or waive fees in an attempt to obtain new customers or additional business from current ones. **To avoid being at a competitive disadvantage** to others, banks should ensure that any vendor it hires not only gives it a fair price, but **that such price is as good as that supplied to other businesses.**

To receive a price guarantee, **get it in writing!** For example, include a provision requiring the vendor to agree that you will receive the service or product at a price as favorable as the vendor has provided to its other customers. Also, consider including a mechanism in the contract allowing re-evaluation of the pricing on a continuous basis to ensure competitive pricing as market conditions evolve. Moreover, since the product or service the vendor is supplying to you may depend upon the vendor receiving a product or service from a third party, the vendor has the opportunity to mark-up expenses on third-party products or services in an attempt to generate a higher profit. Therefore, consider including a provision in your contracts prohibiting the vendor from marking up any fees in excess of the vendor's actual expenses incurred or that provides your bank with the opportunity to review said expenses.

SECURITY CONCERNS

For banks, **security is paramount.** Unfortunately, during tough economic times unscrupulous behavior abounds! While the vendor itself may have a reputation for being trustworthy, there is no guarantee that the same is true for the vendor's employees or contractors. As vendors frequently have access to your and your customers' confidential information, or may even perform services on your premises, be aware of these security issues and implement specific policies and procedures to reduce potential opportunities for dishonest vendor employees and contractors.

While it is not feasible for you to **investigate the background of the vendor's employees or contractors**, you can require the vendor to do so **via the contract.** For instance, you should include a provision in your contracts requiring the vendor to conduct employee background investigations. While it is preferable for the vendor to conduct background investigations on all employees, at a minimum, the vendor should perform investigations on the employees that actually will be providing products or services to your bank or that will have access to your or your customers' confidential information. Typically, background investigations should include verification of prior employment and criminal background checks to ensure that none of the vendor's employees has been convicted of a felony. Drug testing is also common. To ensure proper criminal background checks are performed, it is a suggested practice by the Federal Deposit Insurance Corporation that banks conduct fingerprinting when hiring employees.¹ Finally, if the vendor's employees provide

Banks, like other businesses, rely on third parties to operate certain aspects of their business when the bank cannot effectively or efficiently perform the service or produce the product itself. For instance, by outsourcing certain activities, banks may be able to gain operational or financial efficiencies or increase management's focus on core business functions. While there are numerous issues that need to be considered in a contract negotiation, during tough economic times special consideration should be given to certain provisions, such as pricing, security, continuity of business, confidentiality and insurance, to name a few.

services on your premises, make sure that the vendor is aware of your on-site security rules, and is obligated under the contract to comply with such rules.

BUSINESS CONTINUITY

Many products or services, such as the outsourcing of core processing functions, are critical to a bank's daily operations. **As a bank, you have an obligation to assure the safety, soundness and continuity of essential banking functions.** Accordingly, only vendors that you believe will be in business for the long haul should be used. While there are various ways to determine the financial stability of a vendor, it is still wise to protect yourself contractually. For instance, include a provision in your contracts requiring the vendor to represent and warrant that it is solvent and able to pay its obligations as they become due. Alternatively, you could require the vendor to deliver either a financial certification from the vendor's auditor or financial officer as to the vendor's current financial condition or require that a copy of the vendor's most recent financial statement be sent to you annually. Any of these methods will assist you in determining the financial viability of the vendor.

CONFIDENTIALITY ISSUES

Banks are required to protect their own confidential information as well as their customer's. As a result, it is generally understood that banks and vendors will execute a separate confidentiality and non-disclosure agreement (NDA) or that the vendor contract will contain a confidentiality provision wherein the vendor agrees to maintain the bank's and the bank's customer's information in confidence and provide for procedures for maintaining the safety of such information. Nevertheless, banks do not always consider confidentiality concerns when sending out requests for proposals (RFPs) from prospective vendors.

Price sensitivity resulting from the economic downturn has many banks soliciting RFPs in an attempt to obtain the most

favorable prices. Be aware that RFPs many times contain your bank's confidential information necessary for the vendor to construct a response. As such, prudence dictates that you should require each vendor receiving an RFP to execute an NDA. **The confidentiality provisions in an RFP-associated NDA should be as robust as those associated with a vendor contract itself,** and should expressly require the vendor to agree that any confidential information it obtains will be used for purposes of evaluating the RFP only. As with the typical confidentiality provisions contained in a vendor contract, once the vendor has crafted its response, the RFP-associated NDA should require the return, upon request, of all information that the vendor obtains during the RFP process, and that the vendor immediately discontinue all use of the confidential information obtained during such process.

INSURANCE

Insurance is a risk management tool used to hedge against the risk of loss from foreseeable and unforeseeable occurrences by providing a source for reimbursement against such loss. While individuals obtain insurance from insurance companies, many corporations self-insure (i.e., insure one's property against potential loss by establishing a special fund for such purpose). If the vendor indicates that it intends to self-insure all or a portion of its insurance obligations under the contract, it is imperative that you obtain certain assurances that the vendor is financially able to cover its insurance obligations under the contract. Clearly, when the vendor is a public company as compared to a private company, more information will be readily available to evaluate the vendor's financial strength. No matter how difficult, always make an effort to obtain the necessary information, whether from the vendor itself (e.g., certification from a financial officer) or from other sources, such as consultants/valuation experts, independent auditor reports or other industry sources. After all, the vendor's insurance may be

the primary source of funds available for purposes of indemnifying you and other parties against liability, loss or damage resulting from the vendor's misconduct or negligence.

CONTRACT MANAGEMENT SYSTEM

Once you have negotiated and executed the vendor contracts, you must be able to manage and track these contracts. These contracts contain important information, such as renewal or other critical notice dates that should be organized and reviewed in an efficient manner. While contracts can be tracked manually, it is much more efficient and effective to do so automatically through an automated contract management system. **By using a contract management system, you will avoid monitoring issues that occur when contracts are scattered among branches or departments or different bank employees and, therefore, avoid missing important contract deadlines.**

CONCLUSION

The process of negotiating contracts can be difficult and oftentimes frustrating, but the importance of obtaining terms that are integral to the safe management and operation of your bank cannot be understated. By having the foresight and determination to give due consideration to provisions such as pricing, security, continuity of business, confidentiality and insurance, your bank will be well-positioned to weather any financial storms that may occur. ■



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¹ See *Pre-Employment Background Screening: Guidance on Developing an Effective Pre-Employment Background Screening Process*, FIL 46-2005 (June 2005).