Understanding your vendor management risks

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Agenda

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1) Drivers for vendor management
2) Effective vendor management
3) Vendor management life cycle
4) Ongoing monitoring
5) Key takeaways
6) Questions

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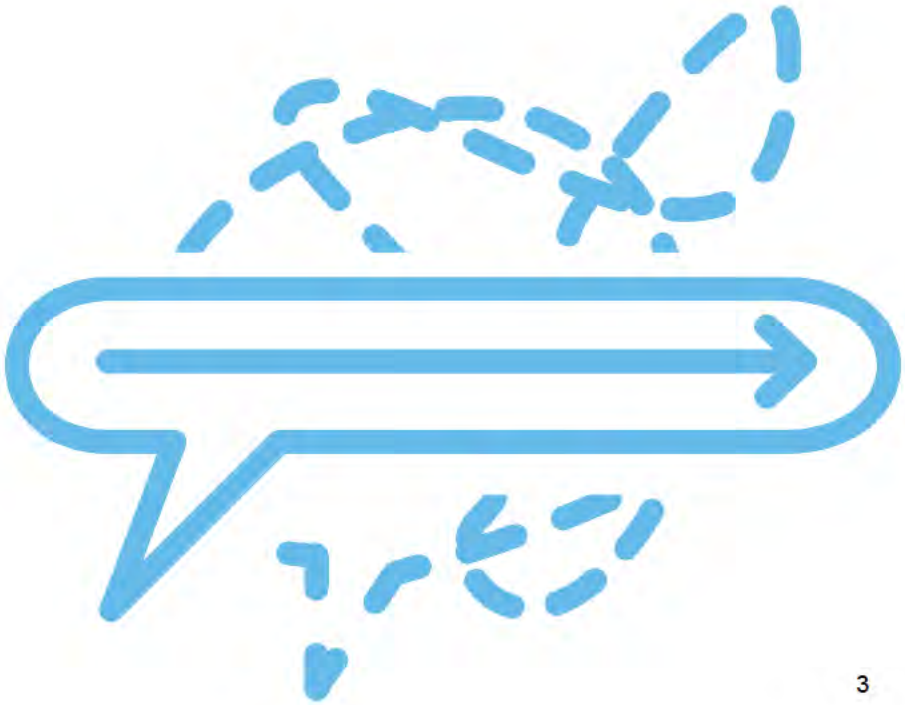
DRIVERS FOR VENDOR MANAGEMENT



Increasing focus

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Two-thirds of companies 'extensively or significantly' rely on vendors

(IIARF)

40% of CEOs expect to develop majority of upcoming innovations with strategic partners

(PwC 2011 Annual Global CEO Survey)

IT is outsourced more than any other function

(Outsourcing Institute)

63% of data breaches in 2013 involved a third-party

(2013 Trustwave Global Security Report)

Increased Risk

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Case study: Multi-billion dollar financial institution

Vendor reliance

- Over 400 vendors
- More than 30 were identified as critical
- Approximately 160 “Critical Applications” identified (operational, financial, security, etc.)
- Approximately 60% hosted onsite (35% running at an offsite hot site)
- 40% Software as a Service (SaaS)

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National Archive and Records Administration (NARA)

Fall 2008: A NARA hard drive containing the names and Social Security Numbers of 76 million U.S. military veterans was sent to a government contractor for repair after it stopped functioning. The vendor determined the drive could not be repaired — so it was sent it out to be scrapped. However, no evidence exists to confirm whether the drive was actually destroyed.

TD Bank

Spring 2012: Vendors lost two unencrypted tapes in transit containing customers' personally identifiable information (PII)

Capital One

Summer 2012: Call-center contractors used deceptive marketing practices to pressure customers into purchasing credit card 'add-on' products over a multi-year period. As a result, the company paid out $150 million in customer refunds and $60 million in fines.

Drivers for vendor risk management

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Business Factors

- Increased number and complexity of vendor relationships
- Informal vendor selection process
- Inability to identify relevant risks by vendor relationship
- Insufficient knowledge of vendor universe
- Inconsistent risk assessment and monitoring practices

Regulatory Focus

- *NAIC*: Annual Financial Reporting Model Regulation, Implementation Guide, Appendix G
- *OCC*: Bulletin 2013-29, Third Party Relationships
- *FINRA*: Rule 3190: Third Party Service Providers
- COSO 2013 Internal Control – Integrated Framework

Drivers for vendor risk management

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Outsourcing business operations does *not* absolve organizations of their responsibilities to manage risk!

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EFFECTIVE VENDOR MANAGEMENT

Effective vendor risk management

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Effective vendor management programs

should…

- Consider organizational strategy
- Evaluate the degree of risk and complexity of each relationship
- Align activities based on evaluation
- Define roles and responsibilities
- Develop reporting mechanisms to facilitate monitoring
- Involves relevant stakeholders

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VENDOR MANAGEMENT LIFE CYCLE

Vendor management life cycle

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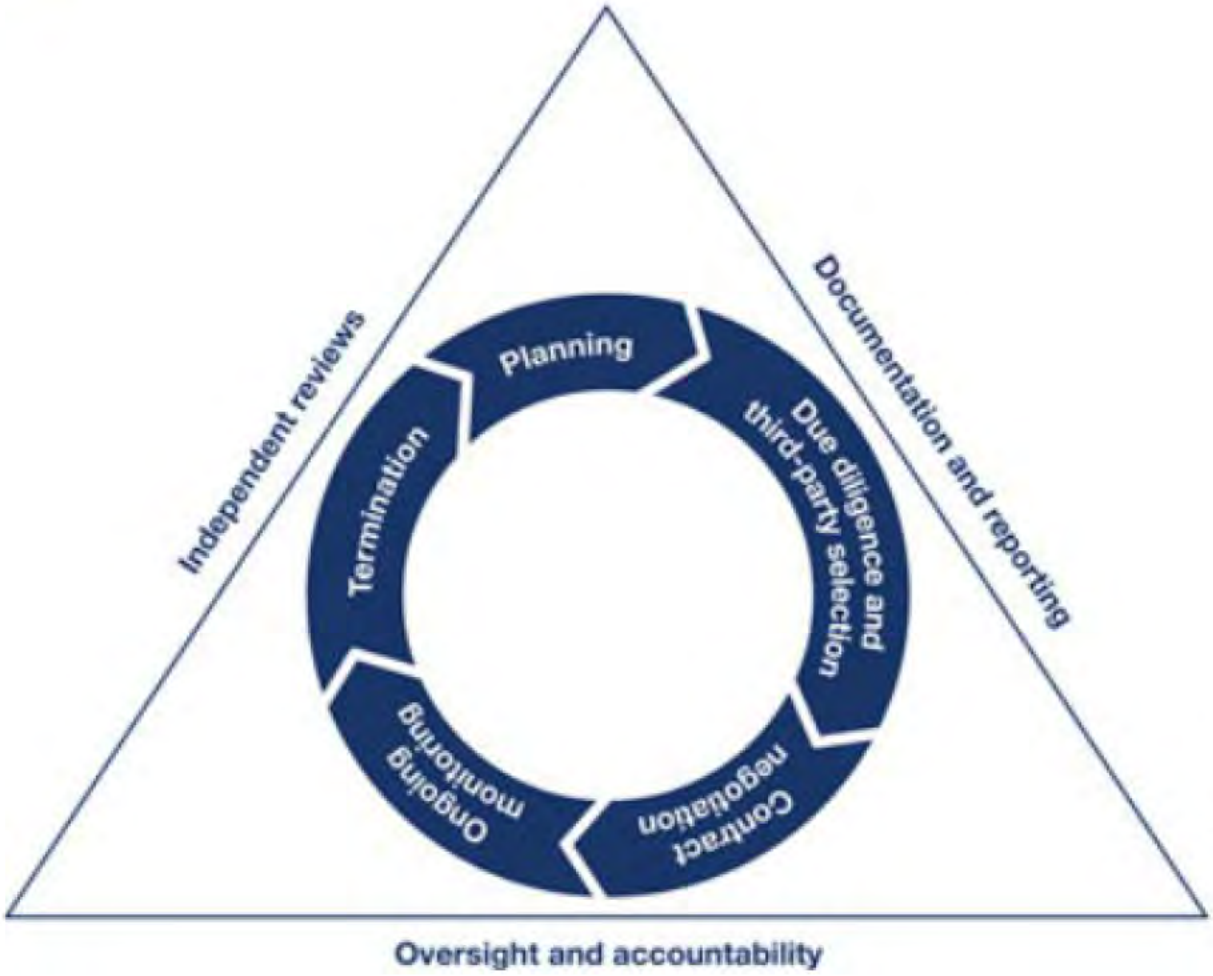

Source: OCC

Vendor management life cycle

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Planning | **Due Diligence** | **Contract Negotiation** | **Ongoing Monitoring** | **Termination**

- Determine the scope of services to be provided
- Assess related vendor risks
- Identify potential vendors
- Issue a Request for Proposal (RFP) or equivalent
- Involve relevant stakeholders:
  - Business Process/Relationship Owner;
  - Subject Matter Expert;
  - IT/Information Security

Vendor management life cycle

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Planning | Due Diligence | Contract Negotiation | Ongoing Monitoring | Termination

> Scale activities based on risk and complexity

> Obtain organizational information for each vendor
- Company history
- Reputational and financial standing
- Risk management program
- Information security practices
- Business continuity / recovery plan
- Any use of sub-contractors (“fourth-party vendors”)

> Evaluate and select chosen service provider

Vendor management life cycle

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Planning | Due Diligence | **Contract Negotiation** | Ongoing Monitoring | Termination

- Use clear, unambiguous language
- Define scope, timing and fees for the arrangement
- Document data confidentiality responsibilities
- Determine any performance measures and/or benchmarks
- Incorporate internal control monitoring requirements (e.g., SOC report, right to audit)

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ONGOING MONITORING

Vendor management life cycle

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Planning | Due Diligence | Contract Negotiation | Ongoing Monitoring | Termination

- Continue to monitor the same areas evaluated during due diligence
  - Periodic risk assessment questionnaires
  - Service-level agreement monitoring
  - Service Organization Control (SOC) examination reports
- Establish criteria for ‘critical vendors’ and increase the frequency and depth of monitoring activities

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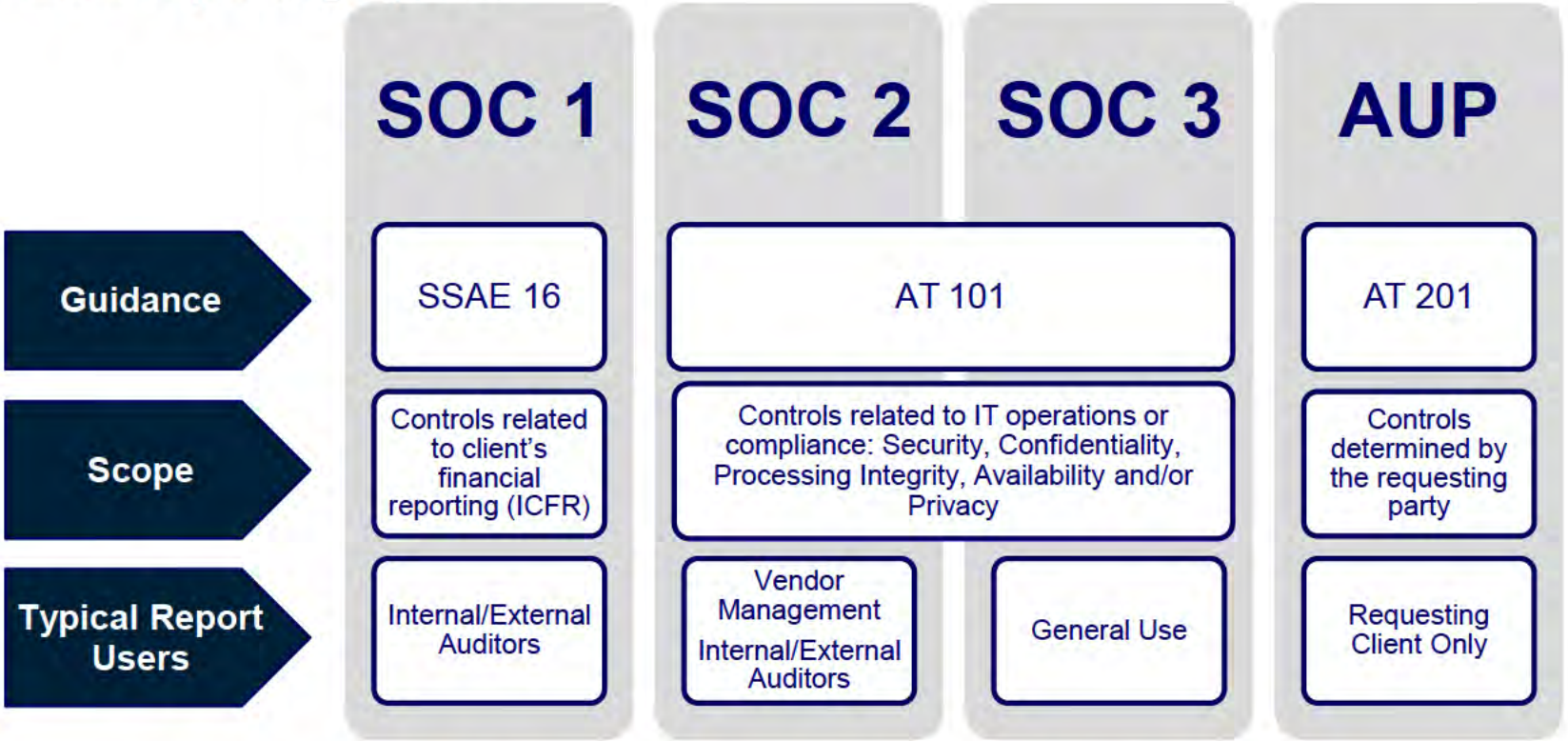
SOC reporting options



Remember: the 'best' option is subjective, and based on the services performed and related third-party risks

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SOC report considerations

- Does the scope of the report address the services provided by the vendor?
- Is the examination period sufficient to provide assurance over the control activities? (Type 1 vs. Type 2)
- How are the Complementary User Entity Controls included by the service organization addressed within your organization?
- Do identified control findings, if any, result in risk to your organization? If so:
  - What actions has the service organization taken to address the findings?
  - What mitigating controls exist either at the service organization or within your organization to address those risks?

Vendor management life cycle

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Planning | Due Diligence | Contract Negotiation | Ongoing Monitoring | Termination

- Understand and document the services performed by the vendor
- Develop a plan to transfer activities to another provider (or bring in-house)
- Evaluate the degree of difficultly and specific risk factors of transition
- Define and monitor data transmission, retention and destruction actions

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KEY TAKEAWAYS

Key takeaways

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- Develop a formal, standardized process for vendor management
- Identify risk considerations by vendor, including criteria for critical vendors
- Tailor due diligence activities based on risk
- Continue risk management for existing vendors through ongoing monitoring
- Determine whether a SOC report will effectively meet monitoring needs

Disclosure

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