

Conducting Due Diligence on Financial Technology Companies

Introduction

In every industry, innovation and evolving customer preference affect how goods and services are delivered. Financial services are no different. As technology evolves, some banks are looking into third-party relationships to enhance the customer experience further.

Reaching out to a company specializing in financial technology (or "fintech") can keep customers' business, increase efficiency, and save your bank money. Of course, it can also introduce risks, but this guide will help you navigate them. Doing so will aid, preserve, and boost your due diligence process.

Using this guide will highlight certain aspects of the due diligence process with fintech companies if you choose to pursue it. Not every type of third-party relationship, risk, or benefit will be present in this guide, so proceed using the information you learned. Regardless, you should reference additional resources (such as federal banking agency guidance). In addition, this resource is not just specific to community banks, so banks of varying sizes may also use this information.

Due diligence is an often overlooked but important component of keeping your bank protected and seeking improvement. This guide will focus on six key due diligence topics of interest.

Business Experience and Qualifications

The first step in assessing a fintech company's experience is taking their experience, goals, and qualifications into consideration. If they meet your needs and can perform their function correctly, they might be compatible.

Business Experience

Their operational history should provide knowledge as to whether they're the right fit for your community bank. Searching through complaints or testimonies from other banking clients is a great point of reference to get a good idea of how they operate. Additional resources can be their public records, media reports, or organizational charts.

Following legal guidelines and meeting customer needs are the bare minimum requirements. Finding any regulatory action against the fintech company is a red flag.

Business Strategies

When considering the fintech company, ask about their methods of operation, management style, and company lifestyle. Company synergy is important towards building a successful third-party relationship. If their brand or personnel seems inconsistent, unprofessional, or unfit for your needs, try looking elsewhere.

It also helps to inquire about their strategic plans and what it means for their company. If they are going through huge changes, such as launching new products, new acquisitions, or joint ventures, make sure it won't interfere with their ability to complete their own business with you.

Qualifications of Leadership

Acquiring background information of their staff, executive board, and owners will give you further insight into whether they are reputable. On their website, they usually have information about their backgrounds. Further digging can lead you to their resource plans and if it will affect their operations.

Financial Conditions

Long-term financial success is a good judge of whether they can stay afloat as a business and adequately perform your requirements.

Financial Funding

Financial reports, statements, projections, and forms will tell you how well they have functioned over the years. Consistent numbers will convey whether or not business with them can remain sustainable. Understanding their funding is also imperative as it can give you an idea of their financial situation.

Market Information

Before settling on a certain fintech company, be sure to compare them to other companies in the field and how they operate as well. Public market information is a good resource to see how they are doing competitively. Looking at their client base is also highly significant. If they have large clients, it is a good sign that they can handle large tasks. However, they might also

allocate more assets to that company. Make sure they can maintain another client before deciding.

Legal and Regulatory Compliance

As mentioned earlier, a company's ability to meet its legal and regulatory obligations is a must. Additionally, a company's knowledge about those obligations is a huge feature. Knowing the ins and outs of their business space will make them more efficient as well.

Legal

Looking at certain tax forms, licenses, and other documents will tell you whether or not the company is on top of its operations. Likewise, referring to certain instances like fines, lawsuits, or other run-ins with legal action is a testament to their legal standing.

Regulatory Compliance

Privacy, consumer protection, fair lending, anti-money laundering are just a few of the compliance duties that should be addressed when reviewing your proposed fintech company.

Industry ratings, records of customer complaints, and marketing details will disclose their company's practices.

Risk Management and Control Processes

Gathering information on the fintech company's control reviews will tell about their ability to comply with risk management/reporting processes. Furthermore, knowing their frequency, nature, and process will provide additional information on the company.

The results will also supplement that information with how their company culture is. So while it is a smaller topic, it can tell you the larger picture of the company, how they operate internally, and whether or not they'll be able to assist you adequately.

Information Security

Before committing to a partnership with a fintech company, understand their practices in managing their cybersecurity risks. Once you enlist their services, they will have access to some of your information as well. If they don't have any groundwork on security, your community bank information may leak out. Evaluate the security measures they take and any incident reports that are filed.

Operational Resilience

When partnering with a fintech company, they will be providing resources that will be crucial to your daily operations. Therefore, ensuring that they can function under any circumstances will be critical in understanding whether the partnership will endure.

Potential information on the subject may stem from sources such as plans for business continuity, disaster recovery, and incident response. Covering your bases with insurance documents and cybersecurity reports also tells how they perform in times of financial or security hardship.

One action that the community bank may propose is a service level agreement. A service level agreement is a document that establishes expectations on their obligations to you.