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FINANCIAL SERVICES
R O U N D T A B L E

KEY CONTRACTUAL CONSIDERATIONS FOR DEVELOPING AN EXIT STRATEGY

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Planning an exit strategy before ever signing a contract with a service provider may seem counterintuitive. However, without a well thought out strategy that is consistent with your overall sourcing strategy, your institution risks becoming locked in to an unsatisfactory relationship or paying more to part ways and minimize operational impact.

An exit strategy helps identify possible risks, defines potential losses and ensures continuity of services. With an exit strategy in hand at the outset of a service provider relationship, your company's needs are incorporated into the contract, ensuring minimum business and customer disruption in the event that the relationship is terminated.

Of equal significance is planning for what happens *after* the relationship ends. For instance, a company should have the flexibility to contract with another third party provider or bring the services back in-house. In determining the components of your exit strategy, consider what you would need from your service provider to make a smooth transition. Also, think about what you would be willing to pay for transition services, if anything.

Types of Terminations

Exit strategies can be deployed for a variety of reasons: normal course of business, lack of performance, change in strategy for either party or merger. In general, the contract should cover:

- **Normal termination**, in which a contract expires.
- **Termination for cause**, which permits the financial institution to exit the contract when problems are not resolved within a required timeframe. This may include a failure to perform or meet service level agreements, quality standards or other contract requirements.
- **Termination for convenience**, which permits cancellation at will. In some instances the party terminating the agreement for convenience may be financially liable. The contract should specify termination fees, if any, as well as responsibilities of the service provider and receiver company through and after the transition period.
- **Termination for regulatory/legislative or supervisory requirements**, which permits cancellation or modification of a contract if required by regulators or changes in regulations, guidelines or law. Examples include but are not limited to:

- The OCC 2001-47 requirement that “the contract should include a provision that enables the bank to terminate the contract, upon reasonable notice and without penalty, in the event that the OCC formally objects to the particular third-party arrangement.”
- USA PATRIOT Act Termination, which requires termination if a service provider/supplier shows up on the OFAC list. This is a new reason for terminating a contract and was enacted by Congress after 9/11 to stop the flow of money going to organizations that are a threat to US security or are involved with money laundering with known terrorist organizations.

Ongoing Service Requirements

An exit strategy should set forth the financial institution’s service requirements for the period during which the parties are transitioning out of the relationship (the “transition” or “wind-down period”). These requirements may include:

- An obligation by the service provider to continue performing the services at the same level of quality for the transition period and to continue to comply with all the obligations in the contract.
- A provision that the service provider give all work product and code to the financial institution at regular intervals during the transition period.
- Specifications for consulting at a reduced hourly rate, upon request.
- Requirements for the provision of parallel services for a certain period, with the right to extend the term as necessary to resolve issues before the final cutover.
- An obligation by the service provider to keep the same service provider team performing services during the transition period.
- Confidentiality on any communications regarding the termination of the relationship.

Data Security and Privacy

Data privacy and security are critical. The exit strategy should consider these issues carefully, including:

- Providing for the immediate transfer of all data that belongs to your institution, including customer information.
- Determining an acceptable method by which the service provider will destroy and remove your company’s proprietary information, including information about the system, operations and business. The exit strategy should identify how the service provider will destroy and remove this sensitive information from all media, ensuring it is not disclosed to other individuals or organizations.
- Recovering and terminating any sublicenses to third-party software and technology, and your institution’s technology licensed to the service provider.
- Taking custody of any tangible property (PCs, servers, network equipment, etc.) provided to the service provider.
- Determining responsibility for compliance with import/export regulations when making final transfers of data and technology.
- Documenting any issues related to intellectual property transfers or protection assistance.

Documentation and Knowledge Transfer

Rigorous documentation and knowledge transfer requirements in the contract will pay dividends when the relationship ends. Be sure to:

- Secure the right to buy the assets, license the software and assume the subcontracts used by the service provider to perform the services.
- Require the service provider to give you access to everything your company will need to maintain service.
- Clearly delineate which party owns the work performed by the service provider and which party is responsible for solidifying the transfer of ownership.

- Fully document the service description for any additional services of the service provider during the transition period (e.g., training your employees or training new service provider personnel).
- Require the service provider to supply a full inventory, architecture, and configuration of servers, routers and other hardware and software involved in service delivery, along with supporting documentation.
- Require the service provider to supply your company with copies of data, procedures, access logs, error logs, documentation and other information that the service provider generates as a part of providing the services. The service provider should also grant your company the right to provide this information to potential successor service providers.

Costs

Transition, termination and timing are a key part of the financial aspects of an exit strategy.

Be sure the contract:

- Will not penalize your institution for an early exit, especially if the termination is due to the service provider's failure to perform adequately.
- Specifies when compensation should be paid and how much, including compensation for any continuing base services and transition activities. For example, payment for transition services may be made at different milestones of the transition or when the transition has been completed successfully. In either case, there may be a monetary bonus to the service provider when the transition services are completed successfully.
- Specifies the return of any pre-paid fees for which services have not been rendered.
- Tailors the compensation arrangement for the transition period in such a way to motivate the service provider to perform.

Personnel

An exit strategy should cover personnel issues, such as:

- The institution's right to hire service provider employees who perform services for you. (This may take the form of a waiver of non-solicitation clause in certain circumstances, such as termination for cause or bankruptcy.)
- Ensuring that service provider personnel and key resources with relevant knowledge and expertise remain on the project and committed during the transition.
- Define the exit-strategy team and its roles, including identifying any situations that should be rehearsed.

Of course, some issues are unforeseeable, so it is a good idea to include an all-encompassing clause. For example, "Service provider shall provide such transition assistance as reasonably requested by Customer." Being both strict and generous in the exit strategy ensures your service provider is motivated to perform.

As with all components of managing an outsourcing relationship, review your exit strategy periodically to ensure it meets your needs and the needs of the evolving business relationship.

About BITS

BITS (www.bitsinfo.org) was created in 1996 to foster the growth and development of electronic financial services and e-commerce for the benefit of financial institutions and their customers. A nonprofit industry consortium that shares membership with The Financial Services Roundtable, BITS seeks to sustain consumer confidence and trust by ensuring the security, privacy and integrity of financial transactions. BITS works as a strategic brain trust to provide intellectual capital and address emerging issues where financial services, technology and commerce intersect, acting quickly

to address problems and galvanize the industry. BITS' activities are driven by the CEOs and their appointees—CIOs, CTOs, Vice Chairmen and Executive Vice Presidents—who make up the BITS Advisory Board and Council.

The BITS IT Service Providers Working Group examines outsourcing risk management issues and publishes industry best practices for IT outsourcing. The group has published two groundbreaking documents for managing IT outsourcing risk: The *BITS Framework for Managing Technology Risk for IT Service Provider Relationships* and the *BITS IT Service Providers Expectations Matrix*. To view these and other BITS documents, visit www.bitsinfo.org and click on “Publications.” For more information about the BITS IT Service Providers Working Group, contact Faith Boettger, faith@fsround.org.