Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

Outsourcing –

Findings and Issues for Discussion

November 2018

1. Introduction

Executive Summary

The Central Bank's mandate includes contributing to financial stability and protecting the interests of consumers. A core element of this mandate is the use of risk-based supervision to challenge the effectiveness of the governance arrangements and risk management practices implemented by financial service providers regulated by the Central Bank ('regulated firms'). Our ongoing programme of supervision seeks to confirm that regulated firms have effective governance, risk management and business continuity processes in place, to mitigate potential risks of financial instability and consumer detriment.

The Central Bank recognises the increasing reliance of many regulated firms on outsourced service providers (OSPs). This includes the use of both intragroup entities and third party OSPs, for the provision of activities and services considered to be central to the successful delivery of regulated firms' strategic objectives. Accordingly, the Central Bank has significantly increased its focus on outsourcing[1] and the management by regulated firms of risks presented by outsourcing arrangements through specific, targeted onsite inspections and wider thematic reviews on outsourcing.

While a number of good practices have been observed, this work has however revealed significant deficiencies in board awareness and understanding of the extent of the reliance within their firms on OSPs. Furthermore, it has highlighted major weaknesses with regard to the related governance and risk management controls and processes in place across all financial sectors. Ultimately, boards and senior management of regulated firms[2] are responsible for the management of outsourcing risk. Significantly, in the case of intragroup outsourcing, it is also their responsibility to understand how and where their firms' systems and data sit within the group priority list. Should something go wrong, it is the boards and senior management of regulated firms that will be held accountable by the Central Bank.

To date, the number of Risk Mitigation Plans (RMPs) issued to regulated firms, reflects the significant remediation required to address control and resilience weaknesses around outsourcing arrangements. The Central Bank continues to engage with regulated firms as it is evident more work is required in this regard.

However, in light of continued concerns and evolving outsourcing trends, the Central Bank embarked upon a wider review of outsourcing across the Irish financial sector. A key part of this review was the 'Cross Sector Survey of Regulated Firms on Outsourced Activities' ("the Survey"), which issued to 185 regulated firms.

The results of the Survey are disappointing. The level of board awareness and quality of governance and risk management remains far from satisfactory. Significant and proactive action is still required by boards and senior management of regulated firms across all sectors to meet minimum supervisory expectations in relation to OSP governance arrangements and risk management controls. Strong business continuity plans

[1] The general term 'outsourcing' is used in this paper in place of other terms which may be used in specific sectors e.g. 'delegation'.

[2] It is important to note that the collective decisions of the board and senior management draw on contributions from a range of individuals with distinct responsibilities.

(BCPs) which incorporate the activities of OSPs, must also be maintained and managed to ensure outsourcing by a regulated firm of any activity does not compromise that firm's resilience. Findings from the Survey and our supervisory engagements suggest that this is not the case in many regulated firms.

This paper is presented in two parts. It sets out the Central Bank's main findings in the context of its outsourcing review and also seeks to begin a discussion with all relevant stakeholders. While the paper is not intended to represent the Central Bank's definitive guidance on outsourcing, Part A focuses on our minimum supervisory expectations as they apply to the specific findings from the Survey and our ongoing supervisory work. Accordingly, the Central Bank expects that any action required to address these findings is reviewed and implemented by the board and risk management functions of all regulated firms.

Part B then discusses a number of key evolving risks across the outsourcing landscape. It also (i) sets out a number of key questions which must be considered and actioned by the risk management functions of regulated firms and (ii) presents a number of questions that the Central Bank wishes to discuss with regulated firms and other relevant stakeholders. Submissions are welcome in this regard as this discussion will further inform the Central Bank's perspective as to whether additional policy or guidance is required on this subject. Further details can be found in the 'Going Forward' section of this paper.

In summary, the observations contained in this paper are largely based on ongoing supervisory work carried out by the Central Bank, together with the findings of the Survey. They are also supported by some additional research conducted on our behalf by Pricewaterhouse Coopers (PwC). Further detail, including the next steps, are set out in the subsequent sections of the paper.

Purpose

As outlined in the executive summary, the Central Bank has noted a significant rise in the use of outsourcing by regulated firms in Ireland. This is supported by the results of its recent Survey as well as ongoing supervisory engagements, including specific outsourcing risk assessments conducted by supervisors, thematic reviews and onsite inspections. However, both the Survey and the outcomes of supervisory engagements, also point to common weaknesses in the current risk management approach of regulated firms to outsourcing across the financial services industry. These observations highlight the need to ensure outsourcing risk is a core priority within the risk management strategies of all regulated firms engaged in outsourcing activity. Therefore, the purpose of this paper is twofold:

Part A – Central Bank Findings and Expectations.

Part A sets out our findings and observations, most of which are not new and have been the subject of previous supervisory engagement with regulated firms across the different financial services sectors. Implementation by regulated firms of relevant outsourcing regulatory requirements and other guidance has been mixed. The findings point to particular weaknesses in the areas of governance, risk management and business continuity management. Therefore, the first objective of this paper is to highlight to regulated firms, the most obvious and minimum supervisory expectations around the management of outsourcing risks and focuses on the most basic areas of responsibility for the boards and senior management of any regulated firm operating in the Irish financial services industry. It is important to note that these expectations are set out specifically in relation to the key findings and observations which have emerged from the Survey and our ongoing supervisory work and which are outlined in this paper. These expectations are not intended to be read as definitive guidance on the wide-ranging topic of outsourcing, nor should they be interpreted as an exhaustive list of requirements with which regulated firms must comply. Regulated firms must at all times look to the relevant legislation, regulatory requirements, standards and guidance to ascertain their statutory obligations.

Part B – Key Risks & Evolving Trends – For Discussion

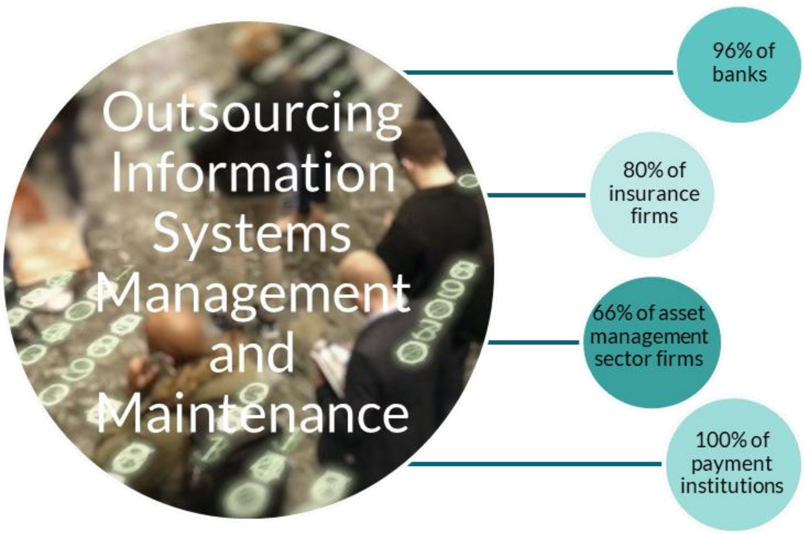
Part B examines some of the key risks and evolving trends associated with outsourcing, and key issues that regulated firms must consider in order to mitigate these risks effectively. In this regard, the second objective of this paper is to promote industry-wide engagement by inviting feedback and discussion on these matters. The 'industry view', including those of regulated firms, their respective representative bodies, outsourced OSPs and other market participants is important to ensure that a consistent and appropriate level of awareness, understanding, management and mitigation of outsourcing risk is developed and maintained across the entire Irish financial services industry.

It is important to emphasise that this paper does not seek to address all outsourcing risks, but focusses on the key risks and issues considered by the Central Bank as requiring closest attention at this time, based on our findings. It is acknowledged that the evolution of the range, scope and profile of outsourcing activity is continuous. In that context, it is imperative that effective outsourcing risk management principles and measures are applied to all outsourced services, irrespective of the nature of the service/activity.

Background

Outsourcing is a written arrangement of any kind between a regulated financial service provider and a service provider (whether regulated or unregulated) whereby the service provider performs an activity which would otherwise be performed by the regulated firm itself. Recognising the observed growth in the reliance of regulated firms on outsourcing within their business operations, and the consequent elevation of outsourcing risk across the risk registers of many regulated firms, the Central Bank has been increasingly focussed on the effectiveness of the related governance and risk management processes over recent years. The Central Bank has carried out a number of inspections across regulated sectors on the effectiveness and capabilities of regulated firms' management of outsourcing and of outsourced activities. The insights gained from this ongoing supervisory work and the related and consistent themes emerging in the risk mitigation actions issued to firms across all sectors, coupled with the results of the Survey, have identified a number of key risk areas which are set out in this paper.

Similarly, the Central Bank recognises the increasing role of technology reflected in the recent rapid growth in the number of fintech (financial technology) and regtech (regulatory technology) firms, and the use of cloud service providers (CSPs) for regulated firms. The increase in the outsourcing of core IT activities is a key concern for the Central Bank as it potentially raises the risks to the resilience of individual regulated firms, and consequently to both the domestic Irish financial system and the wider EU market in which such firms are operating. The extent of outsourcing of IT systems management and maintenance as identified by the Survey is shown below.



Market fragmentation is an increasing feature of the financial sector and has created an environment in which regulated firms need to regularly consider their own organisational structures. This can often result in an expansion by a regulated firm of its risk appetite to facilitate an increased utilisation of outsourcing to meet its business needs. This is particularly important when considering the impact of Brexit on the landscape of the Irish financial services industry in the near term. The current level of authorisation activity reflects the increased number of financial groups and individual firms considering establishing a presence in Ireland. It is emerging that the provision of core financial products and services by these firms, many of which will support business models and activities which may be new to the Irish financial services industry, will in many cases be reliant on OSPs. As such it is evident that dependence on outsourcing is a significant feature of both the current and evolving financial services landscape. This further highlights the need for all financial services industry participants to carefully consider the key outsourcing risks and evolving trends discussed in Part B of this paper.

Methodology

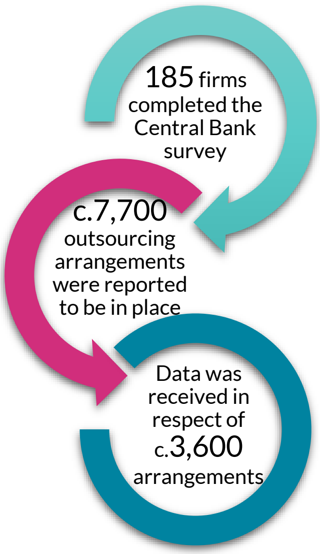
Input for this paper was provided from a number of sources, as follows:

1. **Findings from supervisory engagements with regulated firms.**

   A 'stocktake' of relevant supervisory engagements from the last number of years was conducted and assessed for relevance, including information from Themed Inspections, Full-Risk Assessments and Targeted Risks Assessments. The findings revealed deficiencies in the governance and risk management practices applied to some outsourcing arrangements. These deficiencies were evidenced in firms across sectors and the Central Bank identified the need to acquire a deeper understanding of the outsourcing activity being carried out in regulated firms.

2. **Cross Sector Survey of Regulated Firms' Outsourcing Activity.**

   In order to get a strong, overall view of the levels of outsourcing activity currently being carried out across the Irish financial services industry, the Central Bank issued the Survey to a representative group of regulated firms across the financial services industry[3]. The Survey was completed by 185 regulated firms (18 banks, 82 asset management sector firms[4], 83 insurance firms, 2 payment institutions). Only regulated firms with high, medium high or medium low PRISM impact ratings[5] were surveyed. No credit unions were surveyed, however the findings of other pieces of supervisory work on outsourcing in credit unions support the findings and observations set out in this paper.



[3] It is important to note that survey-related statistical data referenced throughout this paper was generated from Responses received from regulated firms. This data, therefore, may be limited by (i) the likelihood that errors and omissions in the provision of information may exist and (ii) the interpretation of questions which may have differed across the financial services industry.
[4] Asset management sector firms, refers to firms supervised by the Central Bank's Asset Management Supervision Directorate, including MiFID investment firms and Fund Service Providers.
[5] PRISM is the Probability Risk and Impact SysteM used by the Central Bank to conduct risk-based supervision. PRISM uses metrics to assign impact ratings to regulated firms which determines the intensity of supervisory engagement those regulated firms receive. For more information please see: PRISM Explained

The objective of the Survey was to gather cross-sectoral data on;

- the current pattern of outsourcing across regulated firms;
- the extent to which outsourced activities are critical or important[6];
- how regulated firms control outsourcing risks;
- the nature and extent of any potential concentration risk;
- the extent of chain outsourcing;
- the extent of offshoring and any potential country risk;
- the extent to which sensitive data is stored/processed by OSPs.

The survey results were analysed to establish a cross-sectoral baseline view of outsourcing activities and related risks in regulated firms. The 185 survey respondents reported having a collective total of c. 7,700 outsourcing arrangements in place and the Central Bank received data in respect of c. 3,600 arrangements[7]. The survey results also provided an understanding of the potential systemic risks[8] to which the financial services industry may be exposed as a result of outsourcing.

3. **Research on other industries/sectors and jurisdictions.**

The Central Bank engaged the services of PricewaterhouseCoopers (PwC) to provide insights into the management of outsourcing risk in other industries/sectors[9] and regulatory jurisdictions, and any best practice observed in that regard. The observations and information PwC has provided supports the analysis and commentary set out in this paper. As such, the supervisory expectations set out in this paper reflect current best practice in outsourcing risk management, and having regard to the likely future development of outsourcing and emerging outsourcing risk management practices in other sectors.

The Central Bank is satisfied that the survey findings and ongoing supervisory observations are representative of the Irish financial services industry as a whole. Coupled with the PwC research, it is highly likely that the risks and other issues identified by the Central Bank are relevant for all regulated firms where outsourcing is a feature of their operations. Therefore, these observations and issues arising require careful consideration, monitoring and management on an industry wide basis.

Key Findings

The results of the Survey and findings from our supervisory engagements, point to common weaknesses in the current practices of regulated firms in their approach to outsourcing. While all of the issues did not

[6] The term 'critical or important' is used in this paper and replaces the terms 'material' and 'critical' that were used in the Survey. The use of the term 'critical or important' is in line with MiFID, PSD2 and the EBA Draft Guidelines on Outsourcing Arrangements and is used only for the purpose of identifying services, activities or functions under outsourcing arrangements.

[7] The survey required regulated firms to provide details of their top 50 critical or important arrangements. Not all regulated firms surveyed had 50 outsourcing arrangements therefore the Central Bank received data in respect of c. 3,600 arrangements. Only two payment institutions where included in the Survey.

[8] In the context of outsourcing, systemic risk may arise whereby outsourcing risks materialise to the extent that the provision of necessary financial products or services by the financial services sector is significantly impaired.

[9] Non-financial services including Pharmaceutical, Telecommunications and Technology.

arise in respect of any one regulated firm, these are industry wide findings, suggesting that outsourcing risk is not being considered as a core priority within many regulated firms. Failure to improve the standards of management of outsourced activities is likely to generate operational risk levels that are not only unacceptable to the Central Bank, but also we expect, outside the risk appetite of regulated firms operating in the financial services industry.

The key findings include significant risk management deficiencies, on a widespread basis, in respect of a number of aspects of outsourcing risk management, that will be addressed in Part A and which have been grouped under the core functions of governance, risk management and business continuity management:

Governance

- **Board Awareness and Control** - Weaknesses in overall control being exercised at board level, with many boards not being aware of the scale of outsourcing dependencies and associated risks. (Evidenced by deficiencies identified in various aspects of regulated firms' overall outsourcing risk management frameworks).
- **Outsourcing Strategy & Policy** - weaknesses in or absence of outsourcing policies that adhere to relevant regulations and guidelines. In addition, the Central Bank has observed increases in the scale of outsourcing, including outsourcing of key roles and functions which must be considered and managed as part of regulated firms' overall outsourcing strategy.
- **Responsibility and Oversight** - Failure to implement a coordinated risk management approach to the responsibility for and oversight of outsourcing arrangements.
- **Contractual Arrangements** - Failure to put in place appropriate contractual arrangements supported by service level agreements (SLAs).

Risk Management

- **Risk Assessments** - Significant lack of comprehensive initial outsourcing risk assessments and failure to conduct periodic updates of risk assessments.
- **Due Diligence** - Failure to conduct and/ or refresh periodically, appropriate due diligence, both financial and operational, in respect of third party OSPs and intragroup entities.
- **Assessment of Criticality or Importance of Outsourced Functions** - Failure to determine and track the criticality or importance of proposed arrangements. In addition, instances where there was a failure to identify certain arrangements as 'Outsourcing' and hence not applying the appropriate risk management controls to these arrangements.
- **Monitoring and Management** - Failure to devote appropriate resources to suitable monitoring, management and on-site inspection arrangements relating to outsourced activities.
- **Skills & Knowledge** - Failure to retain appropriate skills in house for oversight of outsourcing arrangements and or repatriation or substitution of services, if required.

Business Continuity Management

- **Business Continuity Testing** - Failure to test and periodically retest business continuity arrangements.
- **Deficiencies Identified in Testing Outcomes** - Where testing of business continuity arrangements has been conducted, deficiencies identified in testing outcomes.
- **Exit Strategies** - Failure to devise, document and test effective 'exit strategies' or repatriation contingency plans.

The survey data and our ongoing supervisory work have also uncovered a number of evolving trends and risks in outsourcing. These trends are explored in more detail throughout the paper, and Part B focusses specifically on the key evolving risks identified:

Evolving Trends & Risks

- the expansion in the scale and scope of outsourcing;
- a significant increase in outsourcing of risk management and internal control functions;
- intensified outsourcing of IT services connected, but not limited, to contractual engagements with more innovative fintech, regtech and CSPs;
- a large proportion of outsourcing arrangements involving sensitive customer and business data; and
- the significance of concentration risk for some regulated firms, both in terms of concentration of OSPs used by the sector and the geographic locations where these OSPs are located.

Next Steps

As outlined, a number of our findings relate to poor governance and controls around the risk assessment and management of outsourcing, inadequate monitoring and reporting, failure to consider OSPs in business continuity plans and tests, and a lack of exit strategies or contingency planning. Many arrangements involve sensitive customer and business data. All of these issues weaken the resilience of not only the regulated firms operating here, but of the wider financial sector in general given both the growing number of interdependencies and concentrations.

Boards and senior management are responsible for all activities undertaken by their firms. While it is clear that the outsourcing of activities or services is increasingly common, it should also be clear from the above that it is not possible to outsource the risk. Therefore this responsibility includes activities conducted on the firm's behalf by any third party, including any group entity, or where an outsourcing arrangement is in place. This is critical to ensuring the boards of regulated firms fulfil their accountabilities to ensure the security and resilience of a firm's data and services.

Consequently, the Central Bank expects that all regulated firms take appropriate action to address the issues outlined in this paper and can evidence same to the Central Bank if requested. This expectation includes the review by the risk management functions of regulated firms of the outsourcing arrangements already in place, as well as considering any potential new arrangements. Regulated firms are expected to implement the appropriate policies, procedures and controls, or update their existing risk management frameworks to ensure these findings are appropriately considered and adequately managed.

Outsourcing risk will continue to be a key focus of the Central Bank going forward. In addition to our ongoing review, analysis, supervisory engagement and challenge of the effectiveness of the controls and actions implemented by regulated firms, our onsite and inspection engagement planning will include an intensified level of scrutiny around the management of outsourcing across all sectors. The appropriateness of the related governance and risk management frameworks, and the effectiveness of the actions implemented by firms in this regard, will be central to the scoping of future outsourcing thematic reviews and specific onsite inspections.

With regard to Part B of this paper and the intention to facilitate further discussion, we have set out how to submit your feedback towards the end of this paper. Given the extent of the issues which already exist, we look forward to the receipt of constructive and relevant feedback as we consider the appropriateness and effectiveness of the current approach across the sector in meeting the evolving challenge. Our intention is that the issues outlined in this paper and the submissions received will then be discussed at an industry event to be arranged in 2019.

2. Current Regulations and Guidance related to Outsourcing

It is important that regulated firms consider this paper as supplemental to existing sectoral regulations and guidance on outsourcing and other related topics for their sector. It is a regulated firm's responsibility to ensure that it is compliant with all of the relevant laws, regulations and guidelines, including those applicable to outsourcing[10]. Depending on the sector, these include:

Relevant Regulation, Guidance and Reports
Legislation
Central Bank of Ireland AIF Rulebook
Central Bank (Supervision and Enforcement) Act 2013 (Section 48(1))(Investment Firms) Regulations 2017 – S.I. No 604/2017.
Central Bank (Supervision and Enforcement) Act 2013 (Section 48(1)) (Undertakings for Collective Investment in Transferable Securities) Regulations - S.I. No. 420 of 2015, S.I. No 307 of 2016, S.I. No. 344 of 2017
Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive
European Communities (Undertakings for Collective Investment in Transferable Securities) Regulations 2011 – S.1. No 352/2011.
European Union (Alternative Investment Fund Managers) Regulations – S.I. No. 257/2013, S.I. No. 379/2014
European Union (Markets in Financial Instruments) Regulations 2017 – S.I. No. 375/2017.
European Union (Undertakings for Collective Investment in Transferable Securities) (Amendment) Regulations 2016
European Union (Insurance and Reinsurance) Regulations 2015 (Solvency II Regulations)
Central Bank of Ireland Consumer Protection Code 2012
European Union (Payment Services) Regulations 2018
Companies Act 2014
Central Bank of Ireland Fitness and Probity Standards 2014
Regulatory Requirements, Guidance and Reports
Basel Committee on Banking Supervision Principles for the Sound Management of Operational Risk 2011
Central Bank of Ireland Fund Administrators Guidance 2017
Central Bank of Ireland Fund Management Companies - Guidance 2016
Central Bank of Ireland Investment Firms Questions and Answers 5th Edition 2018
Committee of European Banking Supervisors (CEBS)[11] Guidelines on Outsourcing 2006
European Banking Authority Guidelines on Internal Governance under Directive 2013/36/EU 2017
European Banking Authority Recommendations on Outsourcing to Cloud Service Providers 2017
Financial Stability Board Principles for an Effective Risk Appetite Framework 2013
European Insurance and Occupational Pensions Authority Guidelines on Systems of Governance 2016
Central Bank of Ireland Credit Union Handbook 2018
Central Bank of Ireland Cross Industry Guidance in respect of Information Technology and Cybersecurity Risks 2016
Central Bank of Ireland Guidance on Fitness and Probity Standards 2018
Central Bank of Ireland Report on Anti-Money Laundering/Countering the Financing of Terrorism and Financial Sanctions Compliance - Life Insurance Sector 2016, Irish Funds Sector 2015, Banking Sector 2015

[10] Legal Basis – The supervisory expectations set out in this paper do not constitute secondary legislation. Regulated firms must always refer directly to the sectoral legislation in relation to their outsourcing obligations including provisions of financial services legislation and other enactments, including regulations made thereunder, and any code or other legal instrument as the Central Bank may issue from time to time, when ascertaining their statutory obligations. It is a matter for regulated firms to seek legal advice regarding the application of relevant legislation to their particular set of circumstances.
[11] CEBS was succeeded by the EBA on 01 January 2011.

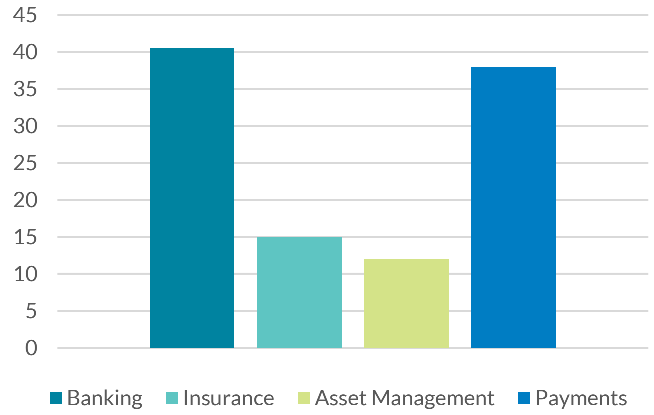
The Central Bank is conscious of ongoing international work regarding outsourcing, e.g. by the European Securities and Markets Authority (ESMA), the European Insurance and Occupational Pensions Authority (EIOPA) and the International Organisation of Securities Commissions (IOSCO), and will remain mindful of same as discussions arising from this paper develop. This includes any new initiatives from any other European Supervisory Authority (ESA) that may also develop or emerge, including the European Banking Authority's (EBA) review of its outsourcing guidelines via its Consultation Paper: EBA Draft Guidelines on Outsourcing Arrangements[12] (EBA Draft Outsourcing Guidelines 2018) which is referenced in this paper. The Central Bank acknowledges that these guidelines are currently in draft format, and will not apply to all sectors. Nevertheless, they are a source of useful information which may be of assistance to other sectors in considering how to comply with their obligations.

[12] This includes the EBA Guidance for the use of cloud service providers by financial institutions.

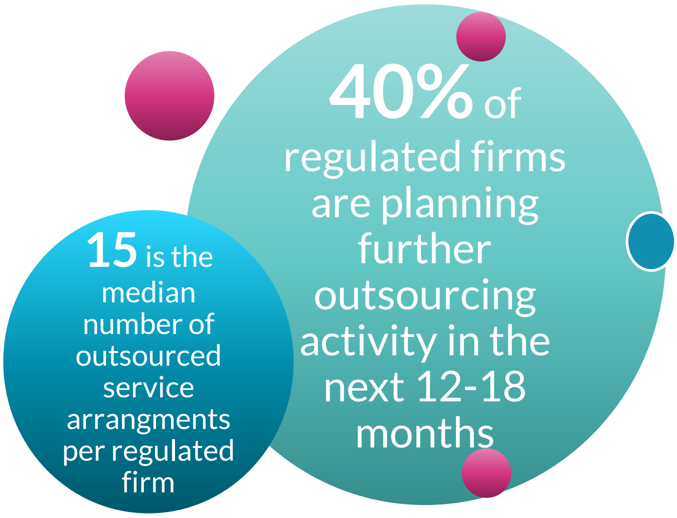
3. Scale and scope of outsourcing activity

An increasing number of regulated firms are relying on OSPs to provide activities and services that are, in many cases, central to the successful delivery of the regulated firm's strategic objectives. Regulated firms are also increasingly being seen to use other companies, whether they are intragroup (where the regulated firm is part of a wider financial group), including sister entities, or third party OSPs to support their operations and/or conduct significant elements of the regulated firm's regulated and unregulated activities. The nature of services and activities provided on an outsourced basis now ranges from those which historically have been widely outsourced to well established OSPs, to other services which could ordinarily be expected to be undertaken directly by the regulated firm itself (e.g. the provision of risk management functions and manpower management).

Chart 1: Median number of outsourcing arrangements per regulated firm



Data collected by the Central Bank via the Survey illustrates the scale of outsourcing activity that is taking place in the financial services industry in Ireland. All regulated firms surveyed were utilising outsourcing. Chart 1 shows that the median number of outsourcing arrangements across all regulated firms surveyed is approximately 15 per regulated firm; however, this varies from 41 in banking to 12 in asset management sector firms. The range of outsourcing arrangements across regulated firms is extensive, with a small number of regulated firms having reported maintaining in excess of 1,000 outsourcing arrangements. Moreover, it is expected that the level of outsourcing will continue to increase, with 40% of regulated firms surveyed by the Central Bank planning to undertake additional outsourcing activity over the next 12-18 months.



3.1 Intragroup Outsourcing V Third Party Outsourcing[13]

Regulated firms are outsourcing activities and services to both intragroup entities and to third party OSPs. Data indicates that the split between service arrangements outsourced to intragroup versus third party OSPs, is roughly 50/50. The evolving operating landscape in the context of Brexit is likely to involve a substantial level of intragroup outsourcing as firms seeking to become

[13] Please note that any reference to Third Party Outsourcing in this paper, does not relate to Third Party Reliance, as set out under section 40 of the Criminal Justice (Money Laundering and Terrorist Financing) Act 2013.

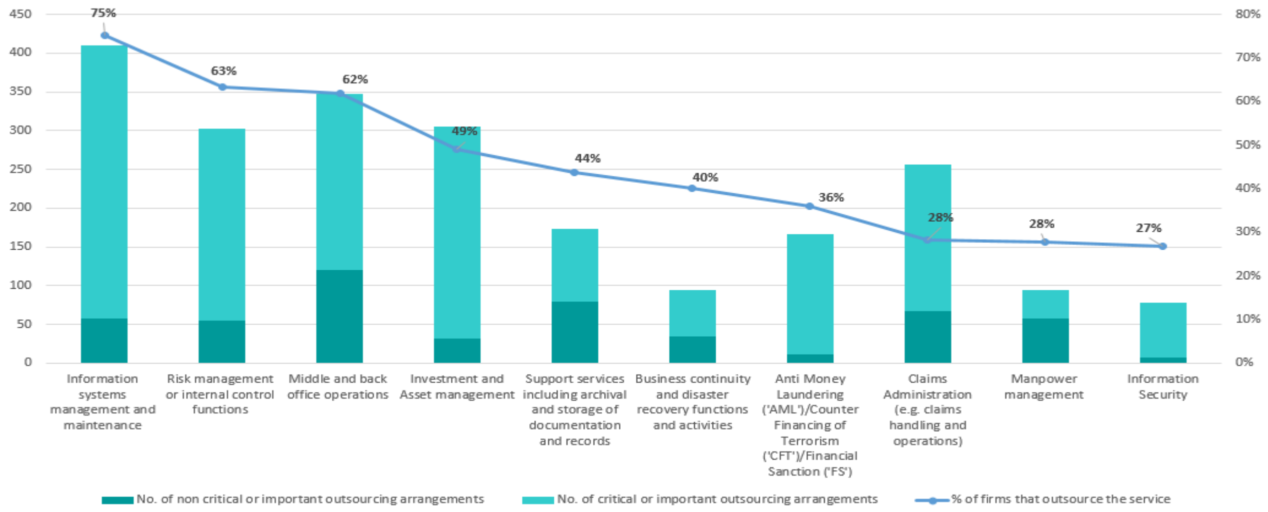
authorised in Ireland look to outsource to existing group entities located in the UK. The Central Bank acknowledges that it can be easier for intragroup outsourcing arrangements to be extended, refined, or adapted to changing needs when compared to third party OSP arrangements and that regulated firms may be able to exercise more control or influence in respect of the management of intragroup outsourcing arrangements; although the opposite may also be the case. However, while the risks associated with both intragroup and third party outsourcing are predominantly the same, intragroup outsourcing also presents unique risks. The Central Bank expects regulated firms to ensure that, in all cases, arrangements are appropriately recorded, understood, monitored and managed. Intragroup outsourcing is not necessarily less risky than outsourcing to an entity outside the group and it is important for regulated firms to note that intragroup outsourcing and third party outsourcing are subject to the same supervisory expectations detailed in this paper.

Finally, with regard to intragroup outsourcing, it is important that regulated firms take into account conflicts of interests that may be caused by outsourcing arrangements. Instances may arise where aspects of some group strategies and priorities are delivered by centralised group OSPs, in a manner that may not be fully compliant with the local regulatory requirements of the regulated firms in question; for example the 'group' may be seeking to increase local market share using a group sales process that is not aligned with local conduct of business or consumer protection rules. Any potential conflicts of interest should be identified and managed accordingly, with regulated firms ensuring that their local legal and regulatory obligations are being fulfilled.

3.2 Services most likely to be outsourced

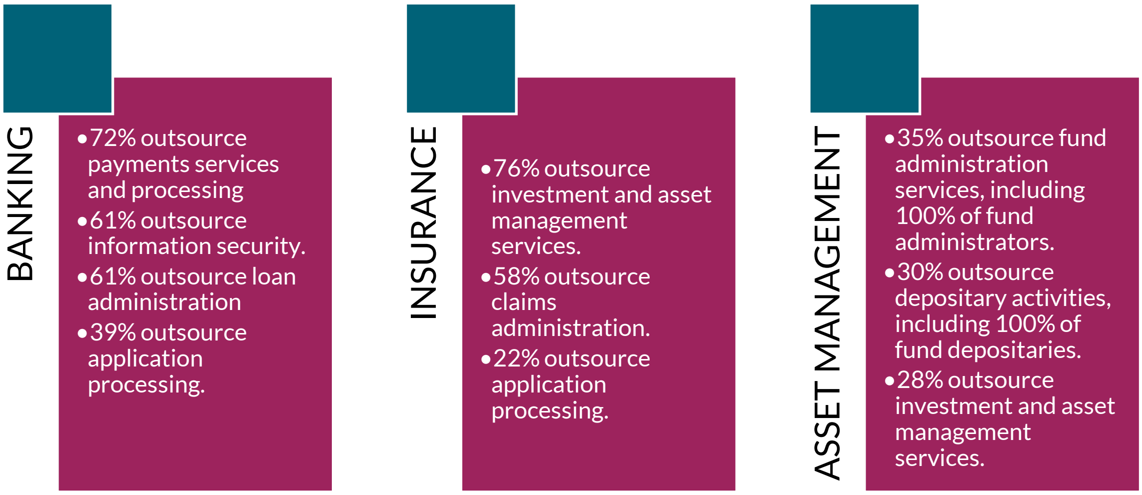
While outsourcing is not a new feature of the financial services landscape, the scope of the activities outsourced in and from Ireland has broadened significantly. The total number of outsourcing arrangements reported by survey respondents is c. 7,700 of which c. 3,600 were deemed to be critical or important by the survey respondents. Chart 2 below highlights the top ten services that are outsourced across regulated firms[14] and the proportion of these services that are deemed critical or important.

Chart 2: Top 10 services outsourced



[14] Chart is based on data collected from the survey.

Chart 2 also represents the number of outsourcing arrangements in place by activity, according to survey respondents and also the percentage of regulated firms from the 185 respondents who outsource that service. While the top three services highlighted in Chart 2 are commonly outsourced across all financial services sectors, the graphic below highlights particular services, where according to the Survey data, a large proportion of firms within each specific sector have outsourcing arrangements in place for that service[15]. The data supporting this graphic indicates that the majority of these services are also deemed critical or important.



3.3 Critical National Infrastructure

Many regulated firms have significant dependencies on other third party vendor relationships in respect of the purchase of services such as telecommunications and power, or for example access to payment and settlement systems. These dependencies pose a potential risk to both individual regulated firms and the financial services industry as a whole. The provision of these services is critical to the delivery of financial services and there is a very high level of infrastructural concentration, which could potentially give rise to systemic risk. It is important that regulated firms consider these systemic risks appropriately within their risk management and BCM strategies, with a view to identifying mitigation techniques focused on ensuring business resilience and continuity of service, in the face of any potential failure of common service providers.

3.4 Evolving areas of outsourcing

There are a number of areas where the Central Bank expects the level of outsourcing to grow rapidly over the coming years, namely; the use of CSPs, and partnerships with fintech and regtech firms.

[15] Payment institutions are not included in this graphic due to the small number of firms surveyed, as 100% of firms surveyed outsourced similar activities.

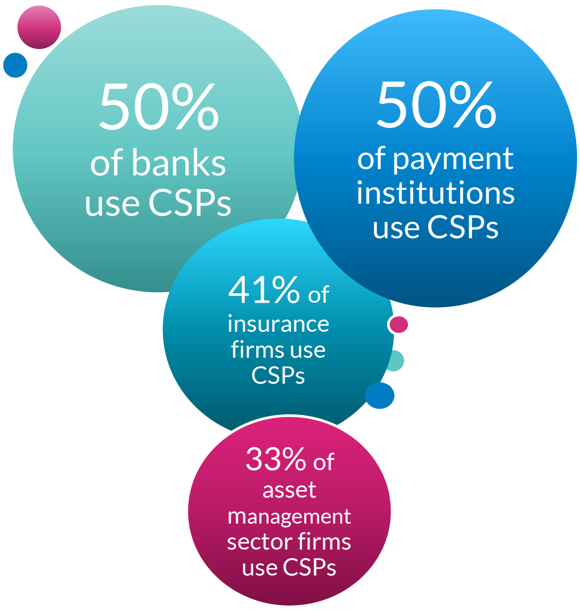
Outsourcing to Cloud Service Providers

Cloud computing is the delivery of computing services—servers, storage, databases, networking, software, analytics and more—over the internet ("the cloud")[16]. Cloud computing has become a prominent service that is outsourced to CSPs who have become increasingly important across many industries, including financial services. Data received from the Survey indicates that 40% of regulated firms use CSPs. Although cloud services can offer a number of advantages, such as economies of scale, flexibility, operational efficiencies and cost-effectiveness, they also raise challenges in terms of data protection, location, security issues, concentration and systemic risk. Challenges may also arise in terms of regulated firms having the necessary knowledge and expertise in order to effectively oversee and challenge such arrangements.

In 2017, the EBA issued recommendations to banks and investment firms on outsourcing to CSPs. The recommendations aim to overcome the high level of uncertainty regarding supervisory expectations that applied to outsourcing to the cloud, which was creating a barrier to institutions using cloud services. These have been integrated into the EBA Draft Outsourcing Guidelines.

Partnerships with 'Fintech' and 'Regtech' Firms

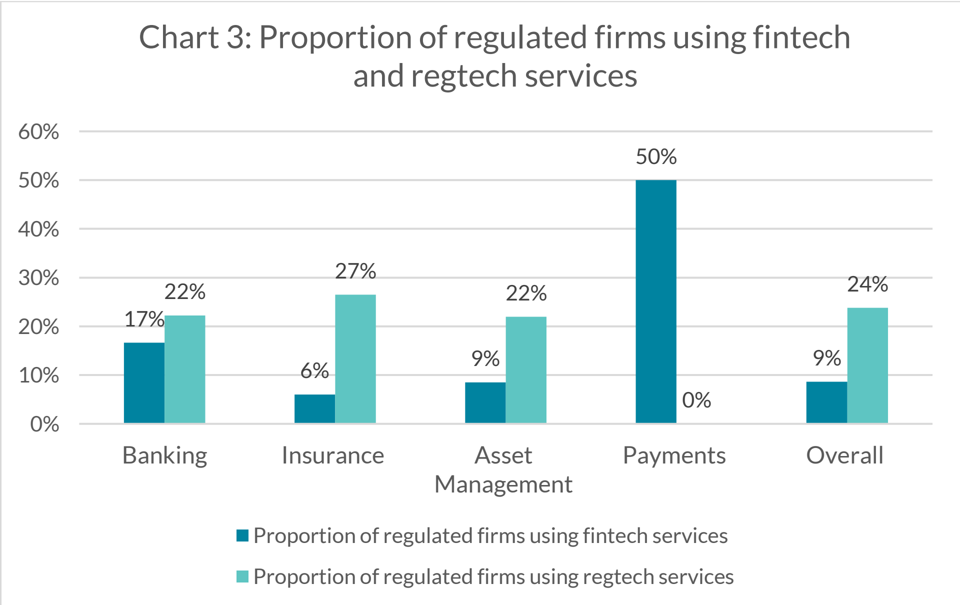
The financial services industry is undergoing significant change in terms of the provision of products and services, with a divergence from activities performed within the traditional silos of banking, insurance, asset management and payments services. Financial services are becoming more modular which has resulted in the emergence of specialist firms that perform a small number of functions that were traditionally performed by a single regulated firm. The financial services industry is witnessing an influx of technology driven innovation by fintechs whose main business objective is to gain market share by meeting the growing expectations and IT capabilities of consumers of financial products and services. Fintechs are typically deemed to be more nimble/agile than the traditional regulated firms and therefore can adapt and react to customers' ever changing needs in a more cost efficient and flexible manner. PwC research estimates that 45% of financial institutions globally are now engaged in partnerships with fintechs[17]. It is worth noting that the limited number of service providers in this growth area may result in concentration risk,



[16] Microsoft Azure Definition
[17] Redrawing the lines: FinTech's growing influence on Financial Services - PwC Global FinTech Report 2017.

which potentially could contribute to systemic cyber risk. Concentration risk is explored further in Section 2 of Part B of this paper.

There are typically three ways in which fintech innovations reach the market:1) start-up firms using innovative technologies become authorised; 2) existing regulated firms develop their own technologies or; 3) existing regulated firms partner with fintechs so that they can use the technologies that they have developed. A total of 9% of regulated firms reported using fintech partnerships as part of their business model when responding to the Survey. However, as shown in the Chart 3 below, the figures vary across sectors, with banking and payment institutions more likely to be engaged with fintechs compared to insurers and asset management sector firms. These reported figures may also be lower than is actually the case as analysis of the survey results suggests that regulated firms may not have regarded 'Strategic Partnerships' or 'Collaborative Strategies' between themselves and fintechs as a form of outsourcing. In this regard, where regulated firms enter into business arrangements with third parties, they must consider whether any inability of that third party to fulfil their part of the service, would prevent the regulated firm from carrying out their critical or important business activities or impair them in providing services to their customers. Such arrangements may fall within the definition of outsourcing and should be treated accordingly. Reported engagement with regtechs is higher than with fintechs, with 23% of regulated firms reporting using regtech services as part of their business model. Regtechs are being utilised more by regulated firms to help manage their compliance with regulatory and supervisory obligations more efficiently and in a more cost effective way.



Results from the 2017 "Industry Research on the Digitalisation of Financial Services", completed by the Central Bank reveal that financial services institutions are considering the introduction of further innovations such as 'Big Data analytics', social media marketing and complaints handling, secure messaging, robotics and biometrics, artificial intelligence/machine learning, distributed ledger technology, smart contracts, fraud analytics, robo-advice, and electronic identity verification[18]. As regulated firms' research into these evolving technologies develops, their engagement and collaboration with fintechs and regtechs is likely to increase; recognising these firms are typically much more advanced in their understanding and development of innovative solutions. According to PwC's "Global FinTech Report 2017", 82% of financial institutions expect to increase and invest more heavily in their partnerships with fintech firms over the next five years. Therefore, as the number of partnerships grows, it is important that regulated firms ensure that they have the appropriate level of oversight and risk management of such partnerships.

[18] Industry Research on the Digitalisation of Financial Services, Central Bank of Ireland, June 2017.

Part A: Management of Outsourcing Arrangements – Central Bank Findings

This section sets out, at a high level, the Central Bank's findings and observations and some minimum supervisory expectations around the management of outsourcing arrangements in the context of the relevant regulatory requirements, standards and guidance. The extent to which regulated firms are utilising outsourcing and the increasing complexity of outsourcing arrangements, means that it is imperative that due consideration is given to governance, risk management and business continuity both at initial inception and throughout the life-cycle of the arrangement.

1. Governance

Robust governance is a key priority for the Central Bank as it determines the effectiveness, or otherwise, of every regulated firm's operations and activities, i.e. from the success of its strategy to the management of its operations, risk profile, control framework and culture. Governance permeates every level and activity of a regulated firm. Therefore governance breakdowns or failures can impact upon the financial soundness of a regulated firm and heighten the risk of operational disruption, consumer detriment and/or threats to the stability of the wider financial system. The Central Bank requires that any regulated firm authorised in Ireland adheres to high standards of governance and does not encourage excessive risk taking. The boards and senior management of regulated firms must demonstrate, as one of their main priorities, the ability to manage and mitigate its material risks including those relating to outsourcing.

The Central Bank has identified weaknesses in a number of aspects of regulated firms' structures and processes designed to manage and oversee outsourcing arrangements. The findings and expectations set out in this regard relate to:

- Board awareness and control
- Outsourcing strategy and policy
- Responsibility and oversight
- Contractual arrangements

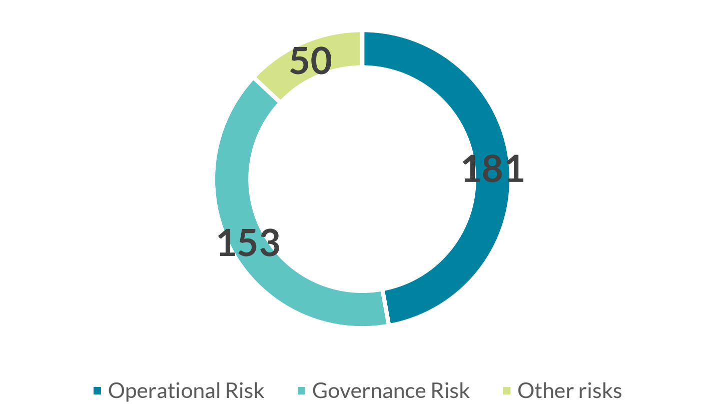
1.1 Board awareness and control

Board awareness and control in relation to outsourcing arises frequently as an area for improvement as part of the Central Bank's supervisory engagement with regulated firms. Instances have been identified, where the standard of controls, awareness and board oversight across the financial services industry are not consistent with supervisory expectations or, in some cases, relevant requirements and guidelines. Since the inception of PRISM in 2011, almost all outsourcing related risk mitigation plans (RMPs) issued by the Central Bank across sectors, have related to operational or governance risk. This indicates that there is a need for regulated firms, under the direction of their boards, to revisit and apply basic operational risk management and governance practices to outsourcing arrangements. Clear commitment from regulated firms to enhance the governance and operational controls around outsourcing risk to the level expected by relevant regulatory requirements should result in:

- more effective risk management by regulated firms;
- a decline in the outsourcing risk profile across sectors; and
- a subsequent reduction in the need for supervisory intervention.

Supervisors have observed a lack of awareness of the scale of outsourcing arrangements and the consequent level of third party dependencies within many regulated firms, particularly at board level. In a number of individual firms supervisors have seen adequate questioning and challenge of proposals and key outsourcing decisions by board members, however, supervisors have found that overall, regulated firms often do not consider the potential impact of outsourcing on end to end processes when making a decision to outsource. This can lead to unintended consequences including unforeseen disruption to processes, where part of a process is conducted by an OSP, and/or a gap in senior management's awareness of the scale or scope of its outsourcing arrangements. Across the financial services industry, the understanding of outsourced IT systems and related governance is varied. It ranges from good knowledge and practices at board and senior management level, to regulated firms being very dependent on the external IT service suppliers and third party consultants to provide both the IT services themselves and assurance of the effective operation of those services.

Chart 4: Outsourcing RMPs issued since 2011



It has also been observed that the required level of awareness and understanding of outsourcing risks is further hampered by the complexities arising from 'chain-outsourcing' arrangements, for example. Chain outsourcing occurs when OSPs engaged by the regulated firm have themselves outsourced certain related activities to other OSPs. This introduces further challenges to a regulated firm's span of control. Chain outsourcing requires very robust controls to ensure these arrangements do not go unnoticed/unmonitored. This is a matter which is addressed in more detail in Section 4 of Part B of this paper. In addition to these observations, the survey data which is examined in this paper, points to a number of fundamental weaknesses in the management and oversight of outsourcing arrangements. This in itself points to weaknesses in the overall governance and risk management frameworks that boards must ensure are in place and operating effectively in order to manage outsourcing risks.

Governance: Observations

- *There has been an increase in the complexity of outsourcing arrangements which presents a range of risks.*
- *There is a lack of awareness of the scale of outsourcing arrangements and the consequent level of third party dependencies within many firms; including by the boards of those firms.*

In this regard, regulated firms are reminded that the effective management of outsourcing risks remain the responsibility of the regulated firm itself – this is not outsourced to the OSP. Regulated firms must also be able to effectively challenge the quality and performance of outsourced processes, services and activities, and carry out their own risk assessment and ongoing monitoring.

It is important to note that failings in governance and risk management practices in relation to outsourcing can result in supervisory intervention by the Central Bank, ranging from RMPs, directions or other supervisory tools and potentially enforcement in the form of administrative sanctions.

1.2 Strategy and policy for Outsourcing

In order to inform board awareness and control, the Central Bank expects that regulated firms have given due consideration to their outsourcing strategy and can evidence that this is the case. In formulating their strategy, regulated firms should give consideration to areas such as, the extent of outsourcing that they intend to undertake and the types of activities and functions they it will consider outsourcing, bearing in mind the risks to which that outsourcing might expose the regulated firm. They must also be able to clearly evidence how any such risks will be managed and mitigated. This strategy should inform a comprehensive outsourcing policy.

ACCORDING TO THE CENTRAL BANK'S SURVEY

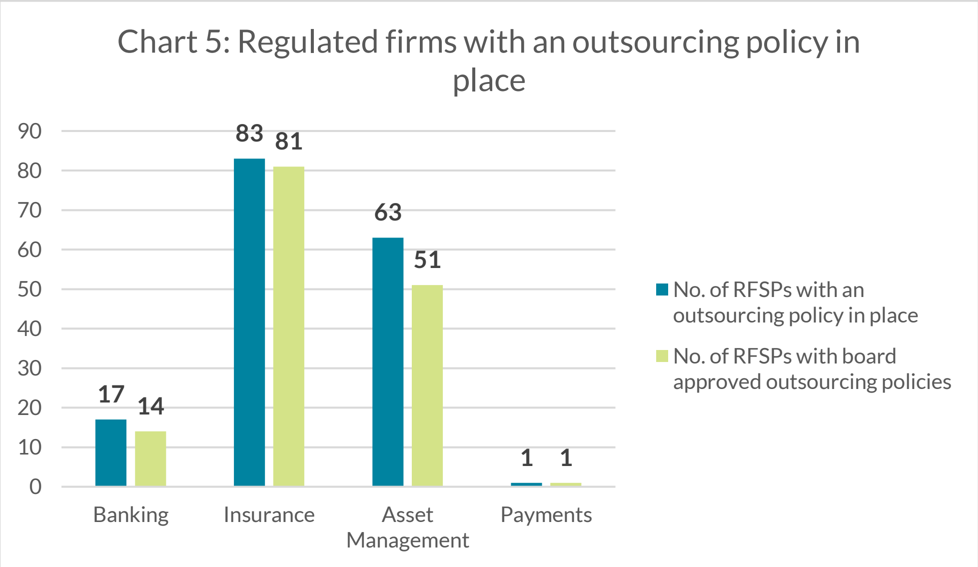
90% of 185 respondents have an Outsourcing Policy in place *and*

90% of policies were signed-off by the board

A total of 90% of regulated firms surveyed reported that they have an outsourcing policy in place and 90% of these policies were said to be signed-off by the board. The insurance sector had the highest positive response rate; with all 83 respondents reporting that they have an outsourcing policy and associated risk management framework in place. The asset management sector firms had the lowest positive response rate; 63 of 82 respondents indicated that they have an outsourcing policy and associated risk management framework in place. Even where regulated firms have responded positively to this element of the Survey, supervisory engagement indicates that a board approved outsourcing policy is not, in itself, evidence of appropriate levels of a board's awareness of outsourcing arrangements. It also does not necessarily mean that the rationale for engaging any particular OSP, or understanding of that OSP's capabilities to effectively deliver an outsourced activity/service has been appropriately represented or understood. Supervisors of the insurance sector, for example, have found, through themed reviews, regulated firms where boards have not seen or approved outsourcing policies and regulated firms where outsourcing policies were not compliant with relevant legislation e.g. Solvency II Regulations.

The 19 asset management sector firms who reported having no outsourcing policy in place had between 1 to 32 outsourcing arrangements. The majority of these regulated firms reported outsourcing services they deem to be critical or important. Regulated firms outsourcing critical or important services with no outsourcing policy and associated risk management framework in place reinforces the Central Bank's concern that oversight of outsourcing arrangements is not appropriately robust. Regulated firms should look to the relevant regulations and guidance (for example those listed in Section 2, page 12) for further information on developing and implementing a comprehensive outsourcing policy.

It is key that regulated firms have a firm-wide outsourcing policy outlining clear lines of responsibility for initial due diligence and ongoing management and review of outsourced arrangements in place. It is expected that such policies incorporate operational oversight and controls, details of the risk management process[19] and the frequency and approach to regular review of the performance levels of OSPs. The outsourcing policy should both enable and require thorough due diligence to be conducted on potential OSPs and ensure a level of consistency in a regulated firm's approach to outsourcing. It should also set out decision points and escalation routes for provision of management information (MI) to the board. This will enable the board to provide sufficient challenge prior to the approval of an arrangement and facilitate the ongoing oversight of arrangements.



Outsourcing risk management/internal control functions

The level of outsourcing of risk management and internal control functions is considered high, with 63% of regulated firms having reported in the Survey that they outsource a risk management and/or control function. The Central Bank requires that the board and senior management of a regulated firm must, at all times, be fully responsible and accountable for the setting of an institution's strategies and policies (including the risk appetite and risk management framework). One of the biggest risks related to outsourcing is loss of visibility and control, therefore regulated firms outsourcing any part of their risk management or internal control functions must ensure that they maintain adequate oversight of these functions. This is explored in more detail in Section 3 of Part B of this paper.

[19] A regulated firm's risk management strategy should take account of its outsourcing policy to ensure that the two are aligned and create no undue impact on each other.

Outsourcing of PCF and CF roles and activities

The Central Bank has noted an increase in the number of PCF/CF roles and activities being outsourced across the financial services sector.

While regulated firms predominantly outsource functions or services, the Central Bank is observing an increase in the number of Pre-Approval Controlled Functions (PCFs) and Controlled Functions (CF) roles and activities being outsourced across the financial services industry. PCFs are roles where Central Bank approval is required before an individual can assume the role. While Central Bank pre-approval is not required for CFs, there are additional responsibilities on both the regulated firm and the holders of these roles.

The Central Bank's Guidance on Fitness and Probity Standards 2018[20] ("the F&P Guidance") outlines requirements in relation to the outsourcing of PCFs and CFs. The Central Bank expects that where any outsourcing of a control function occurs, the regulated firm is in a position to demonstrate that clear governance, responsibility and accountability in respect of the relevant function is retained and monitored within the regulated firm.

Notwithstanding that a regulated firm has entered into an outsourcing arrangement for the performance of such roles, the regulated firm remains responsible for compliance with its obligations. Any outsourcing of PCF or CF roles does not, therefore, diminish the responsibility of the board or senior management in this regard.

Where a regulated firm outsources a PCF or CF role, consideration must also be given to whether this role is being outsourced to a regulated or unregulated entity and to practical issues that may arise, particularly where the individual or OSP is located in an off-shore jurisdiction. Regulated firms are reminded of their related obligations under the F&P Guidance in this regard.

1.3 Responsibility and oversight

Oversight of outsourcing arrangements begins at the arrangement's inception and continues throughout its lifecycle until it has reached an orderly conclusion. When considering and assessing any proposal to outsource, it is essential that regulated firms have an appropriate oversight structure in place. Strong and routine oversight of outsourcing activities, with clearly established lines of responsibility is critical. Effective oversight extends beyond the business line(s) or business area(s) which are affected by an outsourcing arrangement, right up to the board who are ultimately responsible for the regulated firm. Supervisory engagements have highlighted that ownership of outsourcing risk is not always clearly designated/assigned within regulated firms. Instances have been identified, where there was no single owner, unit or committee responsible for outsourcing risk, nor was there a complete and up to date database, or register of all outsourcing and contracted OSPs and arrangements maintained.

It is also important to note that the decision by a regulated firm to engage in outsourcing must not inhibit the regulated firm or the Central Bank from having appropriate access to information, processes and personnel

[20] Guidance on Fitness and Probity Standards, Central Bank of Ireland 2018

in order to gain assurance that activities are being executed and managed appropriately. The Central Bank is aware of cases where regulated firms have been denied access to OSPs, preventing them from carrying out assurance testing. Regulated firms must ensure that contracts for outsourced arrangements stipulate the requirement that regulated firms and their regulators must be given access to carry out the necessary quality assurance and supervisory work[21].

Cross-functional involvement

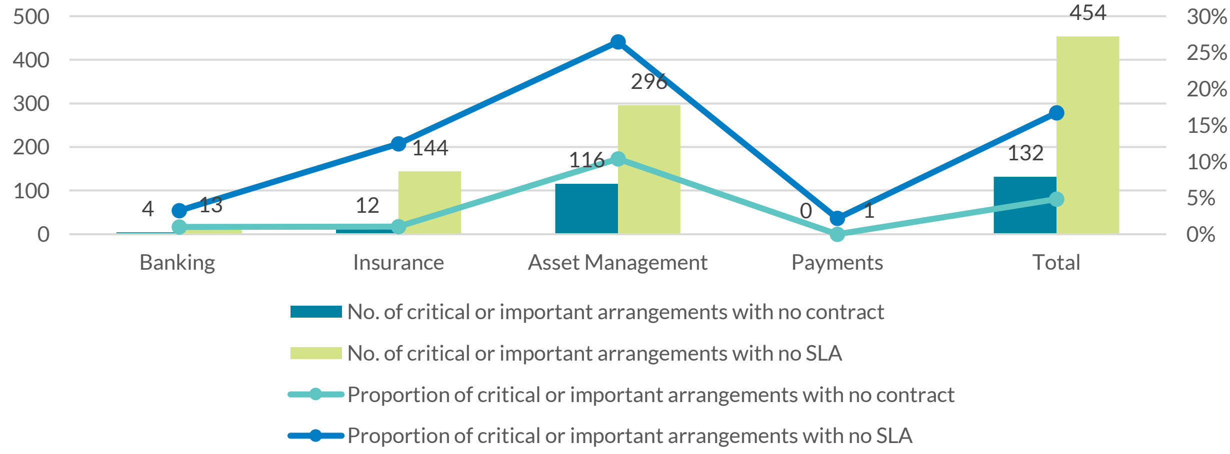
An increasing feature of outsourcing is that a number of different business lines or areas within a regulated firm may have engaged different services from the same OSP. Where such 'cross functional arrangements' exist, regulated firms must consider what additional measures are needed to ensure effective oversight and risk management. As in all cases, it is imperative that there is an ongoing communication of expectations of the OSP, review of service, compliance with SLAs, internal reporting and escalation of issues. Engagement and challenge from all stakeholders within the regulated firm, who are party to the outsourcing process, is fundamental to its success.

1.4 Contractual arrangements

The Survey posed a number of questions in relation to the contractual arrangements in place governing activities being outsourced by regulated firms. Overall regulated firms indicated that 95% of outsourced arrangements deemed critical or important, had written contracts in place; a finding echoed to varying levels in supervisory engagements with firms. Results from the survey in this area ranged from 90% in asset management sector firms to 100% in payment institutions.

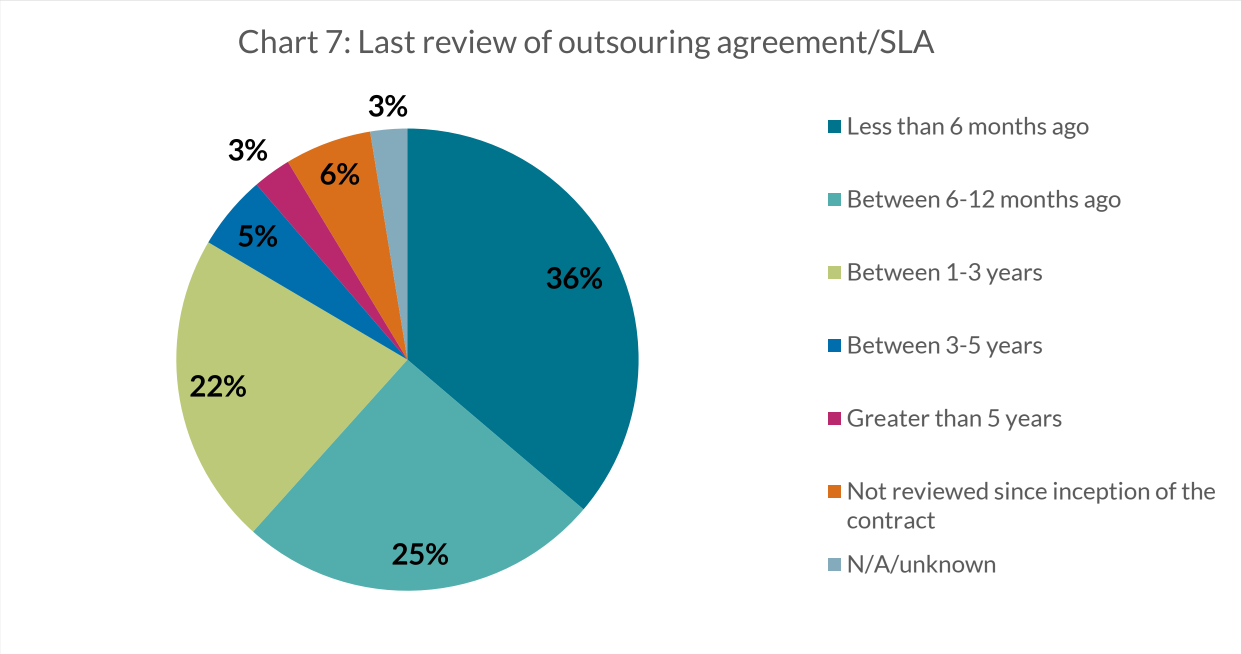
Regulated firms reported that for their critical or important arrangements, only 83% in aggregate had associated SLAs in place. This was made up of 97% in banking 88% in insurance, 74% in asset management sector firms and 98% in payments. An absence of detailed SLAs against which performance can be measured creates a risk that regulated firms do not have appropriate oversight or mechanisms in place to measure performance.

Chart 6: Critical or important outsourcing arrangements with no contract and SLA in place



[21] e.g. CEBS 2006 Guidelines on Outsourcing 8 (g), 8(h) and 11. EBA Draft Outsourcing Guidelines section 10.3.

The Survey also asked questions on the time periods for review of outsourcing agreements/ SLAs. A total of 36% of arrangements had been reviewed within the six months prior to the completion of the Survey, and cumulatively 83% of arrangements had been reviewed within the prior three years. However, it is a concern that for the remaining 17%, the arrangements had not been reviewed in over three years and some had not been reviewed since their inception.



It is important that regulated firms consider whether they have appropriate governance arrangements around the development, signoff and maintenance of SLAs and ensure that their SLAs at a minimum:

- clearly set out the nature, quality and scope of the service to be delivered as well as the roles and responsibilities of the contracting parties;
- include requirements for service levels, availability, and reliability, including measurable performance metrics and remedies for performance shortfalls; and
- be reviewed at least annually and particularly where there are material changes to a regulated firm's business model.

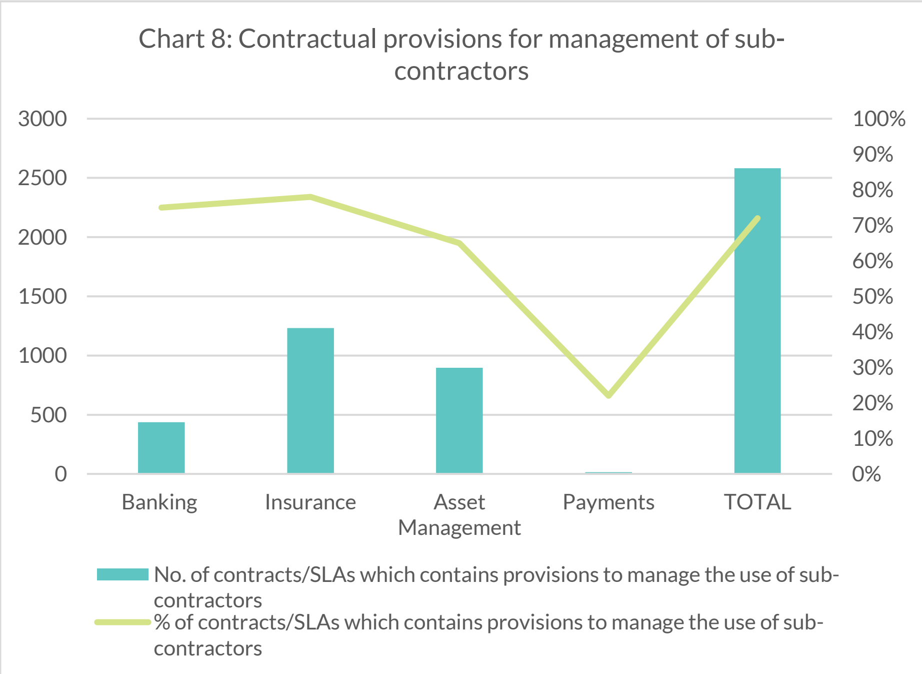
Given the high-profile nature of some significant OSP collapses in recent years and the impact this has had on industries and economies, the importance of robust due diligence of any OSP and the appropriate and regular monitoring of adherence by those OSPs to the agreed service levels has come into sharp focus. The Survey results confirm that regulated firms are not consistently reviewing SLAs on a frequency appropriate to the criticality or importance of the service outsourced. This can lead to increased risk, misplaced expectations and issues around ownership where problems arise or failures occur.

Supervisors have noted both absences and weaknesses of clauses regarding confidential information, quantitative and qualitative performance targets and reporting requirements for material events that may affect an OSP's ability to provide a service, as well as a regulated firm's ability to perform on-going monitoring and challenge of arrangements at board level.

Performance management of OSPs is an ongoing process and regulated firms should consider how best to conduct this. The biggest weaknesses Central Bank supervisors observe in this regard, are related to poor development, documenting and monitoring of key performance indicators (KPIs) that the OSP is or should be measured against. This includes updating KPIs as a result of changing business needs or plans. Clear KPIs need to be established with board level reporting completed at regular intervals. Regulated firms should consider whether they are appropriately engaging with OSPs on an ongoing basis, to the extent that issues are discussed and mitigated in a timely manner. It is important that staff within a regulated firm are aware of the necessary internal escalation routes and decision points when it comes to oversight of OSPs.

Contractual provisions for management of Sub-contractors ("chain outsourcing").

As previously highlighted, the required level of awareness, understanding and management of outsourcing risks can be hampered by the complexities arising from 'chain-outsourcing' arrangements. The Survey included questions on the extent to which contractual arrangements governing outsourcing arrangements include provisions for the management of any sub-contractors party to those arrangements.



Of the arrangements reported on, only 72% of survey respondents in total included such a provision. As outlined in Chart 8 above, this is comprised of 75% in banking, 78% in insurance, 65% in asset management sector firms and just 22% in payments.

As the prevalence of chain outsourcing is seen to be increasing and presents an increased level of risk to outsourcing arrangements, the Central Bank expects that regulated firms give due consideration to this risk and incorporate appropriate risk management controls, including contractual provisions and testing of the performance of the arrangements through the chain of dependencies in order to manage such risks.

Governance Findings - Minimum Supervisory Expectations:

In respect of the governance findings identified, the Central Bank expects at a minimum that:

- *Boards have appropriate oversight and awareness of current and proposed outsourcing arrangements, evidenced by records of discussions and decisions in this regard.*
- *Regulated firms consider the extent and nature of their current and proposed outsourcing and that any strategy devised informs a comprehensive outsourcing policy which is approved by the board.*
- *Regulated firms have appropriate skills and knowledge to effectively oversee outsourcing arrangements; from inception to conclusion, particularly in the case of OSPs using emerging technologies.*
- *Operational oversight of outsourcing risk and outsourcing arrangements is clearly designated to relevant individuals, functions and/or committees, to enable a holistic view of outsourcing to be maintained and reported on.*
- *Regulated firms have robust contracts and SLAs in place with their OSPs.*
- *The outsourcing of any PCF or CF function does not affect the ability of senior management to make decisions and must never result in the delegation of senior management responsibilities.*
- *Outsourcing does not lower the suitability requirements applied to members of a regulated firm's management body, persons responsible for the management of the regulated firm and its key functions holders.*
- *Regulated firms ensure that they are complying with their relevant obligations in relation to any existing or proposed outsourcing of a PCF or CF function.*
- *Regulated firms that outsource the operational tasks of internal control functions for the monitoring and auditing of outsourcing arrangements, ensure the operational tasks are effectively performed, including receiving appropriate reports, and exercise appropriate oversight and are able to manage the risks that are created by outsourcing arrangements.*
- *Third party OSP and intragroup outsourcing arrangements are subject to the same governance and risk management principles.*
- *Similarly, the same governance and risk management requirements are applied to 'partnerships' with fintechs, regtechs and CSPs, as are applied to traditional outsourcing arrangements to ensure all regulatory obligations are being met.*

2. Risk Management

Supervisory thematic reviews of banks undertaken by the Central Bank in 2017 revealed significant gaps in the awareness and understanding of outsourcing risk oversight and monitoring responsibilities. This can result in regulated firms over-relying on the first line of defence for assurance around outsourcing arrangements while the second line, including the risk function, may be largely unaware of outsourced activities and the extent of its responsibilities in this regard. In addition to ensuring that appropriate governance structures are in place, the effective monitoring and mitigation of any risk, including outsourcing risk, requires the development, implementation and robust application of a strong outsourcing risk management framework. A process to regularly monitor risk profiles, including any material exposures to losses, should also be maintained. Complementing this, the OSP should have appropriate internal reporting mechanisms in place, which are mirrored in the regulated firm's relevant business lines and the senior management's reporting to the board. This will support proactive management of the associated risks.

2.1 Risk assessments

Supervisory engagements have highlighted instances where regulated firms have not conducted adequate risk assessments of their outsourced activities or reviewed and updated such risk assessments on a periodic basis, to ensure that they continue to accurately reflect the regulated firm's business. In order to effectively manage outsourcing arrangements, regulated firms must ensure that their risk management framework appropriately captures outsourcing risks. This includes ensuring that risks inherent in all outsourced core products, activities, processes and systems are appropriately identified, assessed and managed. An integral part of risk management is completing risk assessments. This should be a continuous and systematic process in which known and potential risks are considered, identified and analysed and that required mitigating controls are applied. Comprehensive risk assessments are a key tool in enabling appropriate and adequate oversight of outsourced activities.

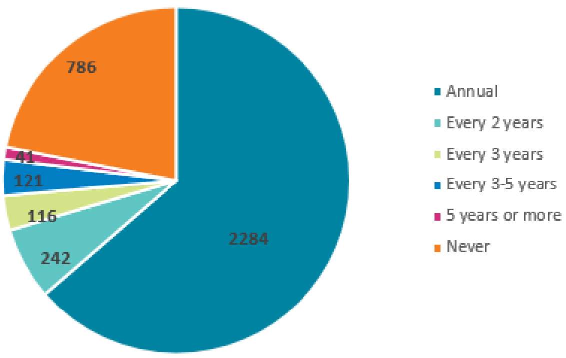
64% of arrangements are subject to an annual due diligence review

2.2 Due diligence

The Survey questioned how frequently regulated firms carry out due diligence reviews on the OSP or sub-contractor after initiation of contract. Chart 9 below shows the responses received in this regard across the four sectors surveyed. While a significant portion of the regulated firms surveyed (64%) responded that due diligence reviews are carried out on an annual basis, it is a concern that 22% of respondents reported that due diligence reviews had never been carried out.

In conducting due diligence on potential OSPs, regulated firms must ensure that risk controls are at least as strong as the controls utilised by the regulated firm itself. Due diligence should also consider whether the OSP can meet its requirements and contractual obligations in relation to service quality and reliability, security and business continuity; in both normal and stressed circumstances. There must be no breach of a regulated firm's risk appetite as a result of a third party OSP activity or failure. This may be avoided by both prior and ongoing assessment of the potential impact of outsourcing arrangements on risk appetite and risk tolerances as well as consideration of scenarios of possible risk events.

Chart 9: Frequency of due diligence reviews on OSPs (per outsourced arrangement)

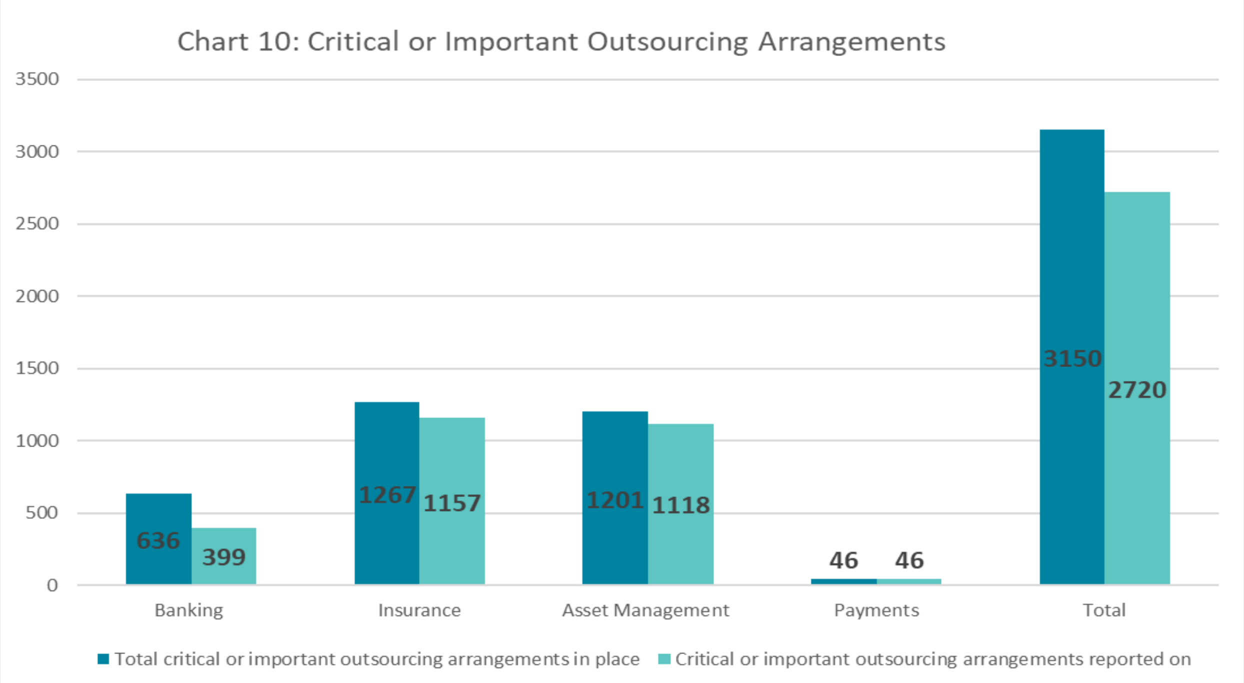


2.3 Outsourcing of critical or important functions

The Survey asked respondents to indicate their total number of critical or important arrangements. According to regulated firms, 41% (3150) of all outsourcing arrangements reported (c.7700) are critical or important in nature. Respondents were also asked to report the number of critical or important arrangements within the top 50 arrangements reported to the Central Bank as part of the Survey. Chart 10 shows that insurance and asset management sector firms surveyed, have close to 1500 arrangements they deem to be critical or important and almost all of these were reported on as part of the survey data gathering. The average number of critical or important arrangements per firm was 15 for both asset management sector firms and insurance, 35 for banking and 23 for payments.

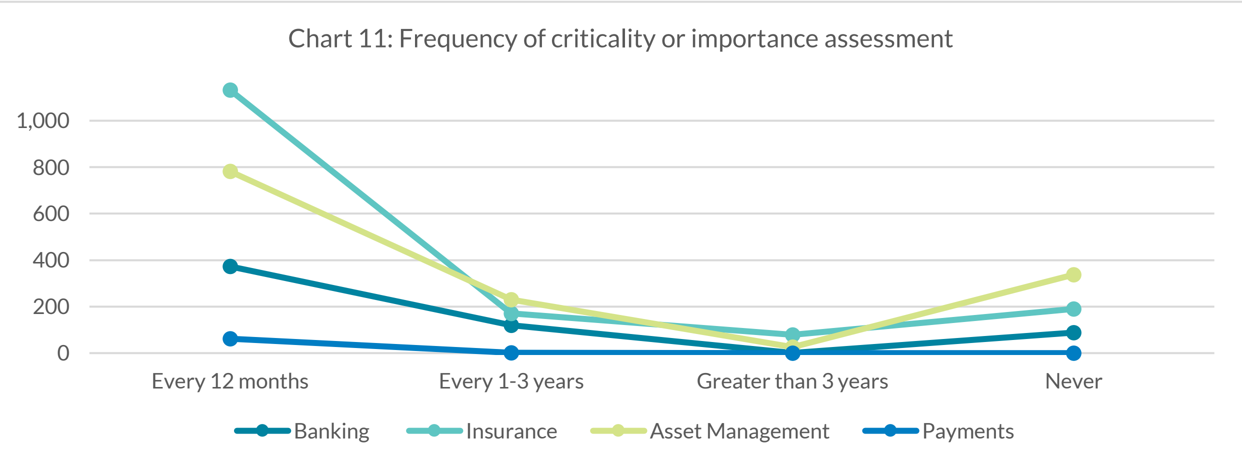
41% of arrangements are critical or important in nature

There are general inconsistencies noted in how regulated firms are determining criticality or importance of outsourcing arrangements. In terms of the criteria used to determine criticality or importance, there was largely a consensus across the banking sector in the use of the CEBS guidelines. However, a number of approaches were reported as being used in both the asset management firm sector and insurance sector to determine criticality or importance. While some regulated firms used either MiFID guidance or EIOPA guidance respectively, this was not consistently applied. Regulated firms may consider the meaning of criticality or importance relative to the size, scale and complexity of the activity being outsourced, if appropriate. The regulations and guidance listed in Section 2, page 12 of this paper provide guidelines for defining a service as critical or important. The Central Bank has observed instances in all sectors where regulated firms failed to designate certain outsourcing arrangements appropriately, most



recently in a 2017 themed review in the banking sector. Therefore, the number of critical or important services reported as outsourced may be underestimated. This is likely to be an area of focus for the Central Bank, with the potential for a follow up review being conducted at some point in the future.

It is important that regulated firms regularly review outsourcing arrangements to ensure that the criticality or importance of services are recorded and reported appropriately. When asked about the frequency of assessing the criticality or importance of outsourced services, 65% of regulated firms across all sectors indicated that this is completed every 12 months. However, Chart 11 shows that in a number of cases services have not been assessed in three years and in more cases, services have never been assessed for criticality or importance.



There is a risk that critical or important services which are outsourced are not being appropriately overseen, monitored and reported on; observed by supervisors particularly in the asset management firm sector and insurance sector. Regulated firms should conduct a cost-benefit analysis of outsourcing critical or important functions relative to their overall capital position. They should also evaluate the efficiencies to be gained from fully or partially outsourcing any function as well as any expected impacts on the business when considering criticality or importance. Appropriate due diligence and risk management controls are key so that a regulated firm is not inadvertently exposed to more significant risks to their business by outsourcing critical or important functions.

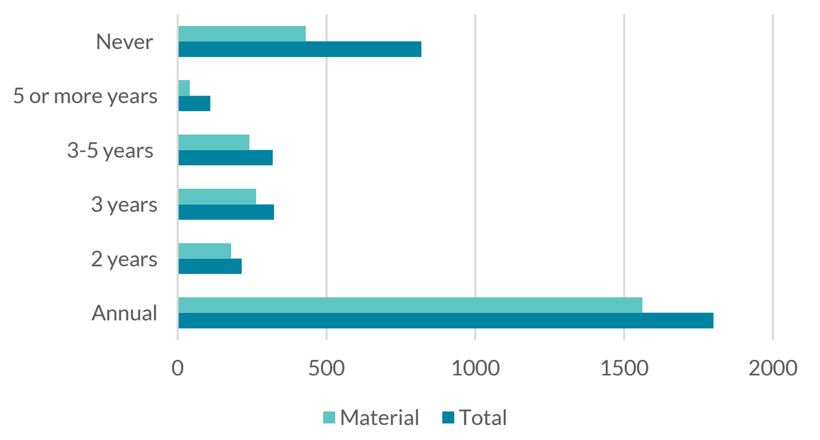
Supervisory engagements have identified another area of concern in relation to classification or outsourcing arrangements whereby, in some instances, regulated firms have not identified certain arrangements as 'Outsourcing' and hence have not applied the appropriate risk management controls to these arrangements. It should be noted that not every provision of a function or service to a regulated financial service provider by a service provider will fall within the definition of outsourcing. Hiring a specialist OSP for example, to provide one-off technical advice or one-off support for compliance, internal audit, accounting, risk management or actuarial functions does not normally constitute outsourcing. However, it may become outsourcing if the regulated financial service provider subsequently relies on that OSP to manage an internal function or service when it is installed or becomes fully operational.

Firms have incorrectly designated some critical or important outsourcing arrangements simply as third party service arrangements.

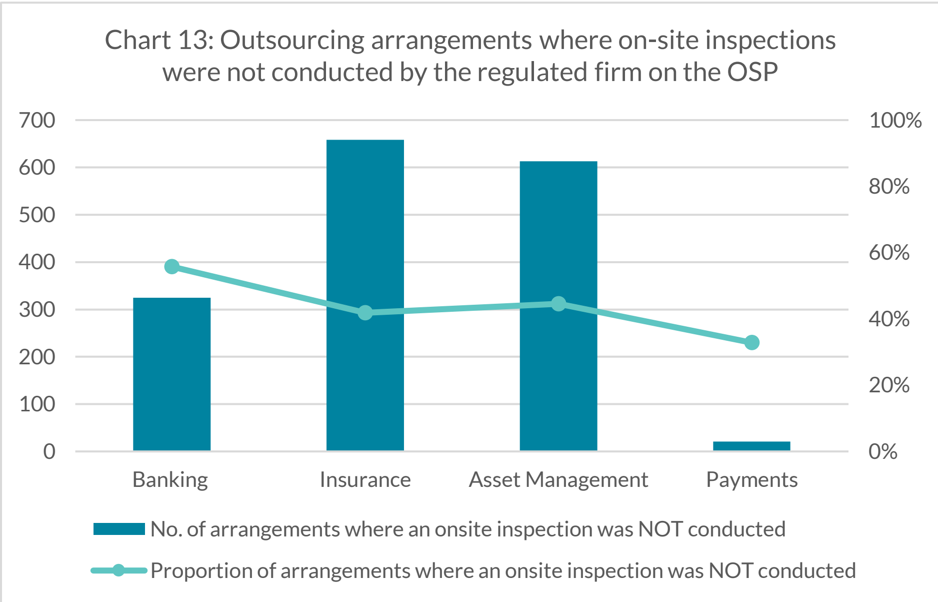
2.4 Monitoring and management

A further question raised in the Survey was in relation to the frequency of the conduct of reviews of the OSP or subcontractor by an independent reviewer. A review of the responses received indicates that while 65% of all OSP arrangements reported on, are reviewed on a frequency of between 1 - 3 years, it is of concern that 35% of OSPs are reviewed less frequently and notably that 23% of these arrangements have never been reviewed. Further analysis of the data in relation to this question indicates that in relation to outsourced functions deemed to be critical or important, 74% are subject to an independent review on a frequency of 1 - 3 years. 26% of respondents indicated that reviews are carried out less frequently, with 16% reporting that an independent review of critical or important outsourced functions had never been carried out.

Chart 12: Last independent review/audit conducted on the OSP (per outsourcing arrangement)



The Survey also asked regulated firms to indicate whether any on-site inspection or review of controls (excluding regulatory inspections) has been conducted on the OSP/sub-contractor. Chart 13 shows the responses across the four sectors to this question. While responses were largely positive in relation to the number of inspections reported as being carried out, it remains a concern that almost half of respondents (45%) either responded that no inspections had been carried out or they did not know, or indeed considered that this was not applicable to them.



2.5 Skills and knowledge

Appropriate skills and knowledge are required by both the OSP and the regulated firm to ensure ongoing effective performance and management of an outsourced service. As part of the transfer of the services to the OSP it is key that there is an appropriate handover from the regulated firm to the OSP to ensure smooth continuance of business as usual activity. Performance management and monitoring processes should be clearly defined and include key risk indicators (KRIs) as 'early warning indicators' of potential future service issues. Regulated firms should consider upskilling their existing employees by means of regular and targeted training to ensure a continued understanding of the outsourced function and the work of the OSP. Outsourcing arrangements must not impair the ability of a regulated firm, including any specialised committees thereof, to carry out its duties. Therefore, it is important that there are sufficient staff with the requisite knowledge to manage the lifecycle of outsourcing arrangements, including having the skills and knowledge, so that functions can either be taken back in-house by the regulated firm or managed through an orderly transition to another provider, if required.

Risk Management Findings - Minimum Supervisory Expectations:

In respect of the risk management findings identified, the Central Bank expects at a minimum that:

- *Regulated firms' risk management framework appropriately considers any outsourcing arrangements.*
- *Regulated firms conduct comprehensive risk assessments in respect of any proposed outsourcing arrangement and that these risk assessments are tailored to take account of specific risks associated with outsourcing, including those set out in this paper.*
- *Regulated firms consider and document the controls to be put in place to minimise exposure to any risks identified and these controls are reflected in the relevant outsourcing contracts.*
- *Regulated firms have a 'criticality and importance of service' methodology that can be applied consistently across all outsourcing decisions and is in line with relevant sectoral regulations and guidance.*
- *The criticality or importance of outsourced service is assessed on an ongoing basis.*
- *Regulated firms maintain sufficient skills and knowledge within the organisation to effectively oversee and challenge the performance of outsourcing arrangements and to ensure that functions can be taken back in-house by the regulated firm or substituted in an orderly manner, if required.*
- *Regulated firms monitor the performance of their OSPs and have mechanisms in place for the escalation and resolution of any issues identified.*
- *Regulated firms retain all responsibility for their strategy and policies where some or all of a risk management function is outsourced.*
- *Regulated firms ensure that their risk management structures are in line with relevant Guidelines.*
- *Regulated firms ensure that the governance and risk management structures they have in place around the outsourcing of IT systems and services are in line with the Central Bank's Cross Industry Guidance in respect of Information Technology and Cybersecurity Risks.*

3. Business Continuity Management

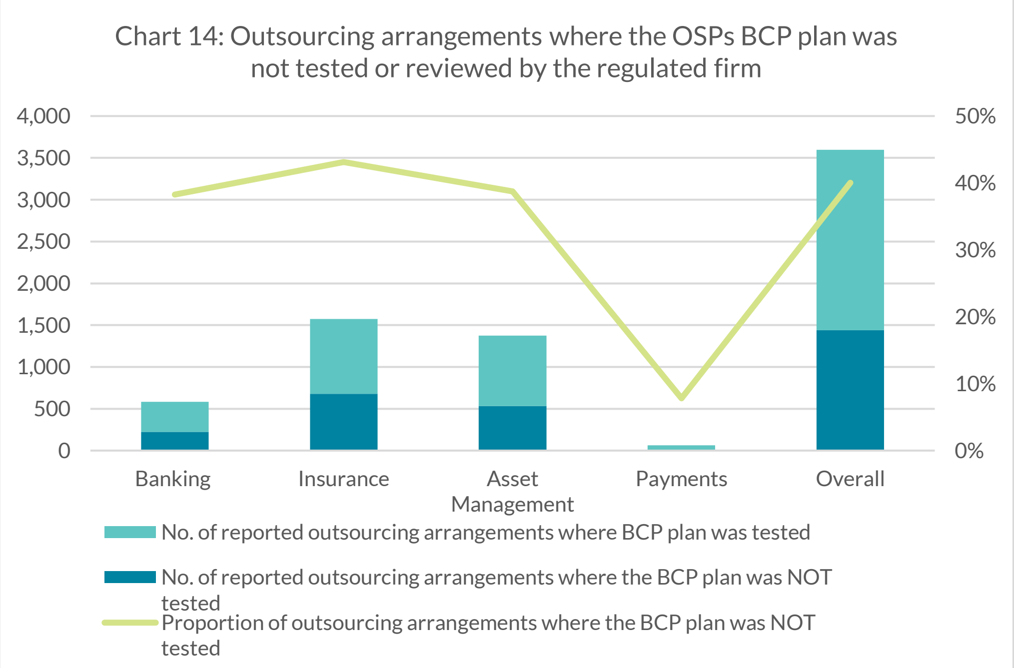
Key to effective governance surrounding any outsourcing arrangement is ensuring continuity of services through robust business continuity management (BCM). An integral part of the BCM process is the regulated firm's resilience to an event occurring. Critical to this is the continuous assessment of the business process and business continuity plans in place, to ensure that controls or other resilience measures keep up with evolving practice and emerging risks and/or issues.

BCPs must be tested on a regular basis, both in the regulated firm and the OSP. All parties must have access to, and participate in, any BCP carried out in respect of the outsourcing arrangement.

The Survey identified a number of deficiencies with respect to BCM in regulated firms, particularly in relation to business continuity testing and having appropriate exit strategies in place. In addition, while the Central Bank, in its ongoing supervisory work, has observed efforts by regulated entities to consider OSPs in their BCM frameworks, supervisors have also seen evidence of a lack of awareness within regulated firms as to whether, or how, their business continuity solutions covered all of their critical systems and data. This indicates that there is a way to go before regulated firms can be satisfied that the BCPs of the OSP are indeed appropriate for their business continuity requirements.

3.1 Business continuity testing

In order to ensure the robustness of a regulated firm's own business continuity plans (BCPs), it is important that regulated firms consider the implications of having outsourced to an OSP and the BCM arrangements that the OSP has in place. However the Survey found that in 40% of the outsourcing arrangements reported, the regulated firm did not test or review the OSP's BCPs.

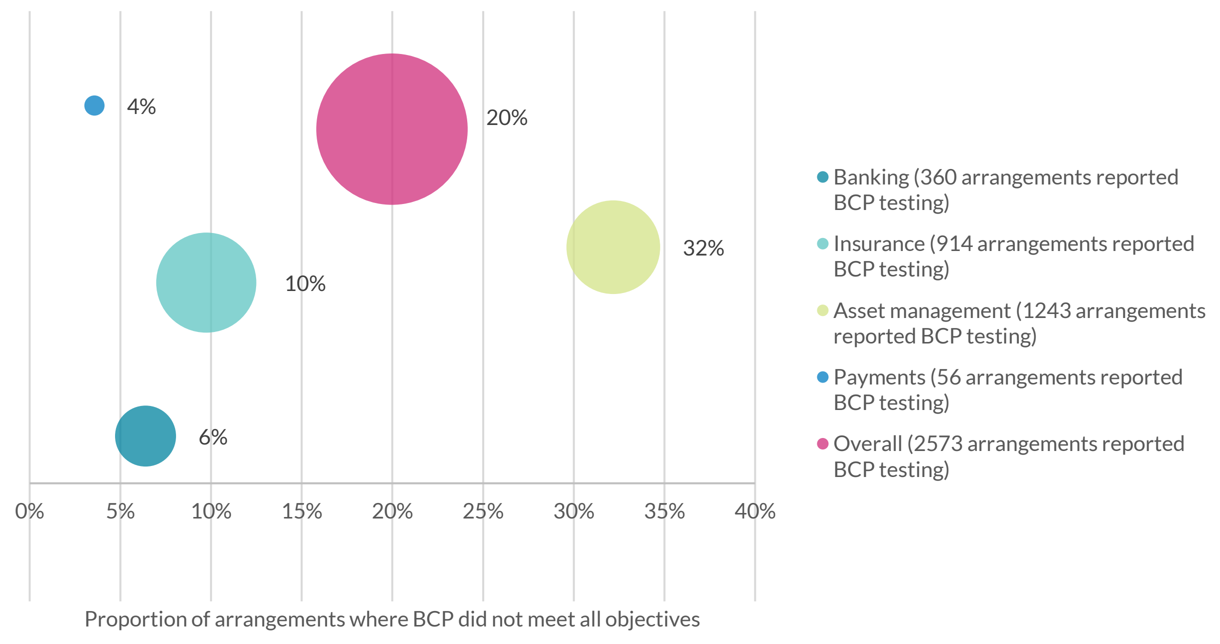


In its ongoing supervisory work, the Central Bank has seen evidence of consistency in the frequency of BCM testing in regulated firms however, there is a distinct lack of awareness of BCM processes in place in OSPs as well as involvement in testing of OSPs BCM processes. This is of concern to the Central Bank and we question how regulated firms satisfy themselves that an appropriate level of support would be provided to it should its OSP have to invoke its BCP. Regulated firms need to ensure that any critical outsourcing arrangement includes a requirement for the OSP to carry out testing of its own business continuity plans on a regular basis. As recommended in the EBA Draft Outsourcing Guidelines (11(87)(c)), regulated firms should have sight of reports on business continuity measures and testing and be informed of any relevant actions or remediations arising as a result of this testing, as appropriate. In addition, when testing their own business continuity plans, regulated firms must ensure that their OSPs are included in the testing of any activities or processes that involve or rely on a service provided by the OSP.

3.2 Deficiencies identified in BCP testing outcomes

The Survey found that where regulated firms did conduct BCP testing with their OSPs, in 20% of arrangements, the OSP did not meet all of the objectives of the BCP test. The results varied across sectors ranging from 4% in payment institutions to 32% in asset management sector firms.

Chart 15: Proportion of arrangements where the OSP did not meet all of the objectives of the BCP test

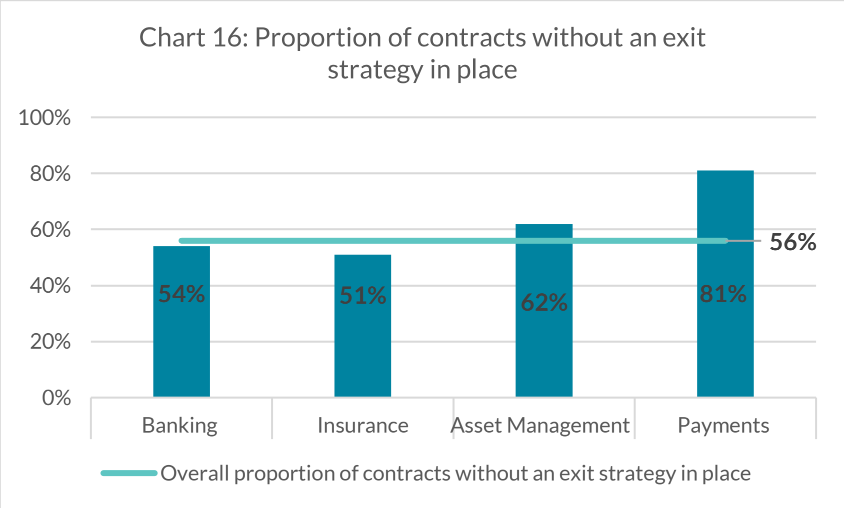


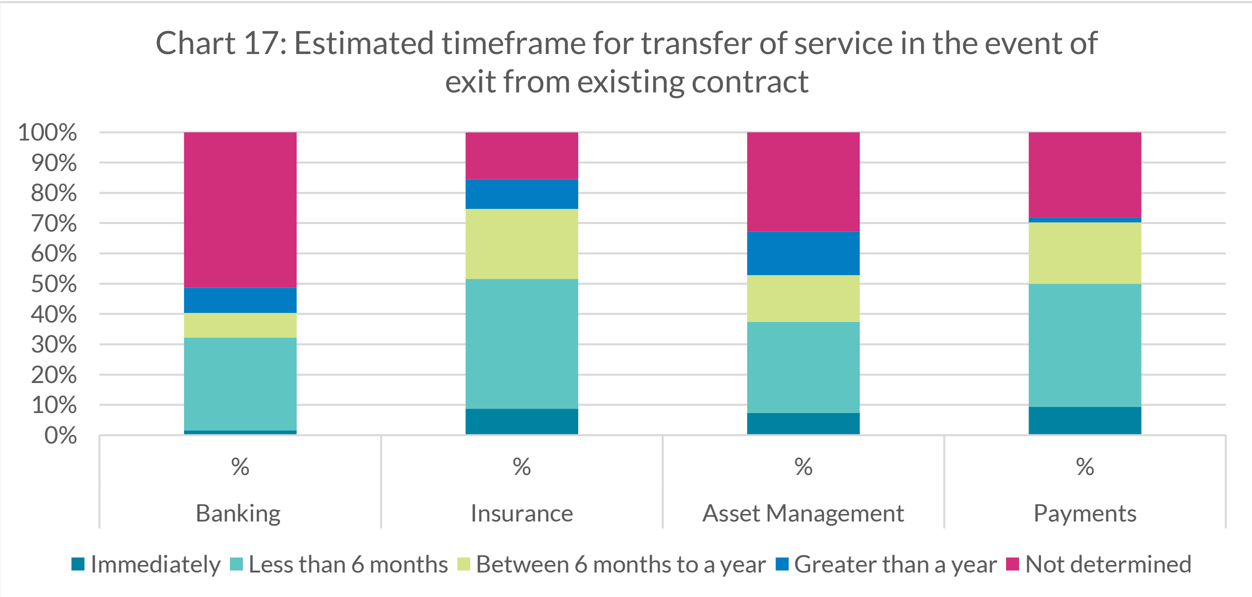
The 2006 CEBS Outsourcing Guidelines (9(3)) state that an outsourcing institution should be prepared to take remedial action if the OSP's performance is inadequate. Regulated firms must ensure that they take measures to address the considerable number of outsourcing arrangements where OSPs are not meeting BCP test objectives.

3.3 Exit Strategies

The resilience of any regulated firm to vulnerabilities presented by outsourcing arrangements will be largely dictated by the effectiveness of the back-up measures in place, including their exit strategies.

Data from the Survey highlights that 56% of contracts for outsourcing arrangements do not have an exit strategy in place. This ranges from 51% of arrangements reported by insurance firms to 81% of arrangements reported by payment institutions. A total of 28% of regulated firms have not determined the timeframe required to transfer services, in the event of an exit from the outsourcing arrangement. This ranges from 15% in insurance to over 50% in banking. 20% of the arrangements have a determined a timeframe for transfer of service of between six months to a year, 41% in less than six months, and 9% immediately.





The 2006 CEBS Outsourcing Guidelines (6(6)(e)) provide that outsourcing institutions should plan and implement arrangements to maintain continuity of their business in the event of an expected or unexpected termination of an outsourcing contract. This includes having a clearly defined exit strategy in place which estimates the timeframe for transfer of service. Regulated firms should also consider and implement contingency arrangements to cover the interim period between invoking an exit strategy and the ultimate transfer. This is particularly important where the timeframe for transfer of service is significant. The regulated firm must ensure that it has appropriate understanding and oversight of the data flows, including how to manage any potential interruption of service or downtime to ensure that critical business functions remain available.

While outsourcing can provide benefits for the regulated firm, for example in terms of efficiencies and cost savings, it also may introduce additional BCM risks to which the entity is exposed. The regulated firm must ensure that these risks are managed in the same manner and to the same degree as if the outsourced activity was performed 'in-house'.

Overall, the board and senior management of a regulated firm remain ultimately responsible for ensuring the appropriateness of the arrangements in place from a resilience and business continuity management (BCM) perspective. The board and senior management must consider the impact of any outsourcing arrangement on existing business continuity plans and must ensure that business continuity plans are updated to reflect the revised service arrangements in place. The Central Bank expects that business continuity plans are tested at regular intervals, and that relevant OSPs are included in any such testing.

Business Continuity Management Findings - Minimum Supervisory Expectations:

In respect of the business continuity management findings identified, the Central Bank expects at a minimum that:

- *BCM is a consideration of regulated firms when proposing to engage the services of an OSP.*
- *Regulated firms ensure that where an outsourcing arrangement is in place, all governance surrounding such an arrangement, including business continuity plans and exit strategies are updated to reflect the variances in service delivery that such an outsourcing arrangement presents.*
- *Regulated firms have back up measures in place and consider, plan and test scenarios which may warrant the transfer of activities to another OSP or back in-house.*
- *Skills and expertise are developed and maintained so that functions can be taken back in-house by the regulated firm or substituted in an orderly manner, if required.*
- *Regulated firms have appropriate exit strategies in place where outsourcing arrangements are utilised and that these strategies allow for a timely and orderly transfer of activities with minimum service disruption.*
- *Regulated firms adhere to the relevant sectoral regulatory requirements and guidelines in relation to BCP and exit strategies, when availing of outsourcing arrangements.*
- *When testing their own business continuity plans, regulated firms ensure that their OSPs are included in the testing of any activities or processes that involve or rely on a service provided by the OSP.*
- *Regulated firms ensure the OSP has a business continuity plan in place, which includes the outsourcing arrangements and that regulated firms ensure that they can participate in the OSPs business continuity plan testing.*
- *Regulated firms regularly review the appropriateness of their business continuity plans and resilience measures in respect of outsourced activities, particularly in the context of new and evolving technologies, trends and risks.*

Conclusion to Part A

The Central Bank has outlined the findings and observations in Part A, in order to draw the attention of regulated firms to common weaknesses identified in relation to the management of outsourcing arrangements from both our supervisory engagements with regulated firms and from the Survey results. The Central Bank expects regulated firms to consider the minimum supervisory expectations set out, in conjunction with the relevant regulations and guidelines applicable to their sector, when assessing the adequacy and effectiveness of measures deployed by regulated firms in the management of any outsourcing arrangements. The Central Bank will continue to engage with regulated firms to assess their governance, risk management and business continuity measures related to outsourcing and will initiate necessary supervisory responses to any weaknesses identified.

Part B: Key Risks and Evolving Trends - for Discussion

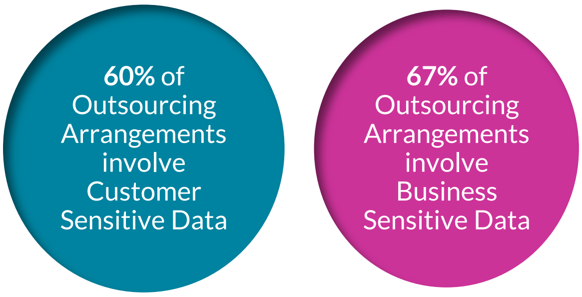
As previously mentioned, Part B of this paper seeks to initiate discussion by asking the financial services industry to consider key risks and evolving trends associated with outsourcing, as identified by the Central Bank. The Central Bank is particularly interested in the approach taken by regulated firms to mitigate these risks.

The following sections set out some of the key risks, both established and emerging, which the Central Bank deems to be most significant in a time when the regulatory landscape continues to evolve and grow. Regulated firms are reminded that the management of these risks is underpinned by robust governance, risk management and business continuity, as outlined in Part A.

In each of the following sections, the Central Bank has set out 'Issues to be addressed by regulated firms', which the Central Bank expects the risk management functions of all regulated firms to action; and 'Questions for discussion with the Central Bank' on which the Central Bank welcomes submissions for further discussion, the process for which is set out at the end of this paper.

1. Sensitive Data Risk

Outsourcing generally involves the handling of a regulated firm's data by a third party in order to execute the services contracted under the outsourcing arrangement. In many cases, this includes sensitive data which is information that is protected against unwarranted disclosure. Access to sensitive data should always be safeguarded.



The Survey data collected by the Central Bank indicates that nearly 60% of the outsourcing arrangements reported involve sensitive customer data and some 67% involve sensitive business data.

There are a number of potential risks that regulated firms must consider and mitigate when either providing access to or transmitting sensitive data to OSPs as part of any outsourcing arrangement. In scenarios where data is being transmitted to the OSP, there is a risk of data loss, alteration, corruption or of unauthorised access while in transit.

Once under OSP management, the risks of unauthorised access to a regulated firm's customer, employee or commercially sensitive data need to be carefully managed to ensure appropriate storage, retention and destruction. Failure to do so could give rise to data breaches, or unauthorised disclosure of information to competitors or the markets. This in turn could damage a regulated firm from a reputational and/or prudential perspective. Sensitive data risk is particularly a concern where the OSP is located in a jurisdiction that is not subject to equivalent data protection laws to that of the regulated firm.

If regulated firms do not retain the appropriate skill sets within their own organisation, they may struggle to understand or verify how their sensitive data is being stored, processed and used by the OSP. Where there is a lack of expertise in relation to the technologies in use, a regulated firm's ability to conduct assurance or reliability testing, or interpret results of testing may be hindered. Regulated firms need to ensure they are capable of conducting and/or evaluating validation testing to ensure their data is subject to the appropriate security standards. This is an increasing concern as regulated firms start to utilise evolving technologies such as cloud services. Some of the specific challenges associated with this are set out in Section 1.1 below.

The Central Bank has observed weaknesses in awareness of risks associated with data storage solutions and an absence of appropriate data protection clauses in outsourcing contracts

In order to manage these risks, it is important that regulated firms devise a robust data management strategy at the outset of any outsourcing arrangement. This strategy should set out the standards and requirements to be applied in respect of the regulated firm's data including back-up and recovery, security protocols and encryption standards, access management and legal requirements.

Research conducted by PwC on behalf of the Central Bank has highlighted that in line with best practice observed in other industries, regulated firms should seek and take account of OSP's data accreditations and attain agreement on the frequency and format of any renewals of these accreditations and of any management information required from the OSP in relation to the service. This should be provided through relevant clauses in the outsourcing contract. In addition, regulated firms should request the right to audit the OSP data storage and management systems to ensure they are aligned with the regulated firm's requirements from a data perspective[22]. Similarly, when data has been successfully transmitted, or access granted to the OSP, regulated firms should ensure that their OSPs have robust policies and procedures in place regarding access management and that their sensitive business data is protected by non-disclosure agreements as part of their contractual arrangements.

These recommendations are in line with the principles set out in the CEBS 2006 Guidelines on Outsourcing, which highlight that regulated firms must ensure that their contractual arrangements with their OSP covers the protection of confidential information, banking secrecy and any other specific provisions relating to handling confidential information. Whenever information is subject to confidentiality rules to which the outsourcing institution must adhere, at least the same level of confidentiality should be ensured by the OSP[23]. The Central Bank has observed weaknesses in this area as part of its supervisory engagements. For example in some banks inspected, the inclusion of clauses to ensure the protection of confidential information have been deemed unsatisfactory by supervisors who have noted that often intragroup arrangements are weaker in this regard than arrangements with third party OSPs.

[22] PwC Report
[23] CEBS 2006 Guidelines on Outsourcing

1.1 Sensitive Data and Cloud Services

As outlined, safeguarding sensitive data is always a necessary consideration in an outsourcing context, particularly given the increased use of third parties for the provision of new technologies and services including cloud computing services. As noted in Section 3.4 of part A, some 40% of regulated firms that participated in the Survey reported that they are using CSPs (a total of 287 arrangements reported), which confirms the prevalence of this evolving area of outsourcing in the financial services industry.

40% of firms surveyed are using cloud services

There is a concern that the complexities of this technology and ability to manage associated risks may be underestimated. A recently published Cloud Security Report which is based on the results of a comprehensive online survey[24] of over 570 cybersecurity and IT professionals to gain a deeper insight into the state of cloud adoption and security challenges, trends and best practices, reports that approximately 20% of the organisations polled have suffered a cloud security incident with a further 20% reporting that they are unware whether or not they suffered a cloud security incident[25].

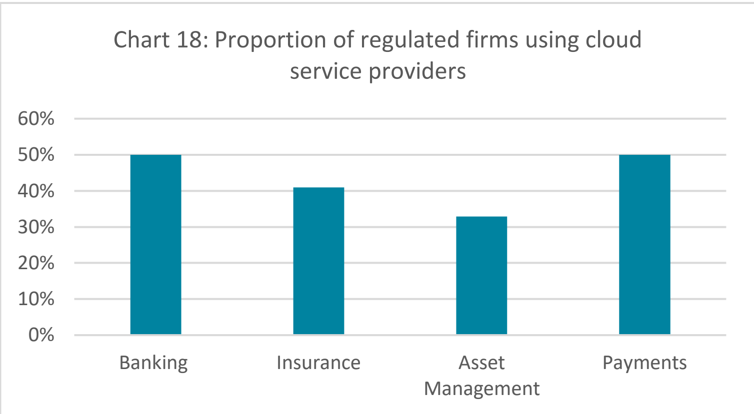


Chart 18: Proportion of regulated firms using cloud service providers

This is an issue which has also emerged as part of the Central Bank's supervisory engagements with regulated firms. For example, in the Central Bank's recently published report on IT risks in credit unions[26], it was noted that 'data classification and full awareness as to the storage of credit union-owned data (including the jurisdiction where it is stored) and the risks associated with its storage was not demonstrated'. There was no evidence of risk assessments being carried out where credit unions engaged cloud storage OSPs. These findings have been mirrored across other sectors resulting in RMPs being issued to regulated firms to mitigate associated risks.

Given the nature of this sensitive data and its associated risks, regulated firms must ensure appropriate controls are in place to ensure the safety and integrity of their data. In the case of outsourcing to CSPs and other outsourcing arrangements that involve the handling or transfer of sensitive data, regulated firms should

[24] Note: this survey was not conducted by the Central Bank and the data does not relate directly to firms regulated by the Central Bank.
[25] 2018 Cloud Security Report
[26] IT Risks in Credit Unions – Thematic Review Findings; January 2018

adopt a risk-based approach to data storage and data processing location(s) and information security considerations[27].

Research conducted by PwC on behalf of the Central Bank has highlighted that with increased adoption of cloud services, there are an increased number of risks. It has been observed that failure of successful implementation of cloud services is largely due to outdated governance and risk frameworks, poor awareness of an organisation's risk appetite, insufficient security and access measures, and a lack of skilled expertise in the retained organisation. Mitigating factors observed are similar to those outlined in more general outsourcing areas and include detailed due diligence on the provider to ensure there is a similar risk appetite, effective change and risk management frameworks, contingency planning, detailed contracts and effective governance. A robust data strategy, as previously referenced, is also particularly important when migrating data to a CSP and this includes the ability to meet all relevant legal and regulatory requirements, as well as identifying any data that cannot be moved. The PwC research also identified other CSP specific risks, which primarily relate to a lack of understanding of cloud technology on the part of regulated firms and how it will be applied to their business models. Maintaining the appropriate skills and knowledge in-house is key to mitigating these risks and all aspects of sensitive data risk arising from outsourcing arrangements.

Issues to be addressed by regulated firms

- *Has the regulated firm ensured that data protection standards applied by their OSPs are aligned to the standards required of the regulated firm?*
- *Has the regulated firm considered the need to ensure consistency of security operations between 'on premises' security and cloud security?*
- *Has the regulated firm considered the need to define standards for configuring cloud services and designing a comprehensive security architecture (identity and access management and governance, data protection and encryption, data loss prevention and security monitoring and operations)?*
- *Has the regulated firm considered the location of data when engaging the services of CSPs?*
- *Has the regulated firm considered the multiple layers in a cloud supply chain when identifying and monitoring risk?*

[27] EBA Draft Outsourcing Guidelines

Questions for discussion with the Central Bank

- *How are regulated firms ensuring that they have sufficient knowledge/ expertise within their own organisation to effectively challenge and gain assurance that their data is being managed securely by OSPs, including CSPs (how and where it is being stored, processed, used, located etc.)?*
- *What issues/ challenges are regulated firms encountering in gaining assurance that their sensitive business and customer data is being managed securely in outsourcing scenarios?*

2. Concentration Risk

The increasing use of outsourcing arrangements is giving rise to growing concentration risk concerns. In an outsourcing context, concentration risk is the probability of loss arising from a lack of diversification[28] of OSPs. This is an aspect which the Central Bank will be monitoring to ensure that any emerging systemic risk is identified and managed accordingly. In the absence of robust contingency planning, concentration risk can result in unplanned service outages, disruption of service to the financial institution customer, brand and reputation damage, and poorly planned transitions to new OSPs. Therefore, regulated firms' risk management frameworks need to include their approach to concentration risk identification, management, and reporting which are appropriate in the context of the nature, size, and complexity of the regulated firm.

83 insurance survey respondents have almost 700 outsourcing arrangements in place with the top 100 OSPs

21 respondents from across asset management sector firms and insurance have 202 arrangements with the same OSP

Data gathered as part of the Survey highlights that some OSPs provide multiple critical and important services to clusters of companies across the Irish financial services industry. These OSPs include global technology companies, business processing entities and professional services companies, payments processing firms, and IT services firms, which are engaged with several different companies across the financial services industry.

On a sectoral level there are also further concentrations. For example:

- In the insurance sector, one OSP provides actuarial services to a large number of companies engaged in similar business lines and activities;
- In the asset management sector several regulated firms are reliant on one OSP for fund administration, anti-money laundering (AML) and middle and back office activity; and
- In the banking sector one OSP provides payment services for several retail banks.

[28] BITS Guide to Concentration Risk in Outsourcing Relationships

There is a significant degree of concentration risk in respect of the provision of particular outsourced critical services. These services include; application processing and back office services; policy administration and associated services; fund administration; depositary services; and NAV calculations; disaster recovery and business continuity services; information security; actuarial services; document archiving services; and card processing.

Concentration risk in cloud services is an emerging and increasingly significant issue requiring careful attention from the individual institutions, but also on an industry level as a systemic issue. This is because large suppliers of IT and cloud services can become a single point of industry failure when many institutions rely on the same provider[29]. In some cases, OSPs may hold significant leverage, due to the specialist nature of the services provided. Regulated firms must ensure that their ability to negotiate and secure robust arrangements with such providers is not hindered, even in scenarios where there are a limited number of OSPs to choose from.

> *Firms need to consider, manage and mitigate against concentration risks; including those arising from outsourcing to a dominant, not easily substitutable, OSP or from outsourcing multiple services to either one, or a related group of OSPs*

It is important to note that concentration risk can arise from outsourcing to intragroup entities, as well as to third parties OSPs. Regardless of whether regulated firms are outsourcing to third party OSPs or intragroup, when assessing the risks of an outsourcing arrangement, regulated firms need to be aware of, manage and mitigate against any potential risks arising from outsourcing to a dominant, non-easily substitutable OSP or from outsourcing multiple services to one, or related OSPs[30]. While the Central Bank acknowledges that there are certain benefits to consolidation of outsourced activities, this can increase concentration risk. Ideally regulated firms should choose multiple OSPs in order to avoid being over-reliant on one provider. Regulated firms should also consider concentration risk exposure, where they are aware of a widespread dependence on a small number of OSPs within their sector. Research across the pharmaceutical, telecommunications, and technology industries points to the use of dual outsourcing arrangements[31], shorter duration contracts and bidding for contracts as ways to encourage more regular review of the outsourced service and to reduce concentration. Regulated firms should consider the appropriateness and application of these practices in respect of outsourced activities.

[29] EBA Draft Outsourcing Guidelines
[30] EBA Draft Outsourcing Guidelines
[31] In order to avoid concentration risk, in the telecommunications industry, a shadow outsourcer is often appointed throughout the life of the contract, ensuring there is not total reliance on one provider – PwC Report.

2.1 Concentration Risk arising from Chain Outsourcing Arrangements

Concentration risk not only arises directly from outsourcing arrangements but also indirectly from any subcontracting or 'Chain Outsourcing' undertaken by the OSP. While a regulated firm may consider it has adequately diversified the delivery of key processes to different OSPs, each of those OSPs may in turn be outsourcing the process, or a key element of the process to the same subcontractor. In this case, a regulated firm may be partially insulated from a failure by one of the OSPs, but remains exposed to failure by the underlying subcontractor[32]. In order to manage and mitigate this risk, the CEBS 2006 Guidelines on Outsourcing[33] recommend that regulated firms should include conditions in the outsourcing contract that require the prior consent of the outsourcing institution to the possibility and modalities of sub-outsourcing.

2.2 Interconnectedness and Systemic Concentration Risk

Complex links among financial market institutions are a hallmark of the modern global financial system. The level of outsourcing and sub-contracting in particular, often to a limited number of OSPs, has led to a web of indirect interlinkages between firms. This may result in systemic concentration risk. The collapse of a UK multinational facilities management and construction firm in early 2018 and its subsequent impact across the UK and Ireland, particularly across government projects, highlights the possible consequences when institutions are overly dependent on a small number of OSPs.

Issues to be addressed by regulated firms

- *Has the regulated firm given consideration to concentration risk prior to entering into new outsourcing arrangements?*
- *Does the regulated firm seek to structure their contracts with OSPs in such a way that other OSPs are not discouraged from bidding for the service ?*
- *Has the regulated firm considered concentration risk in respect of CSPs, particularly where there are a limited number of CSPs available?*
- *Has the regulated firm mapped out the concentration risk they are exposed to from chain outsourcing?*

Questions for discussion with the Central Bank

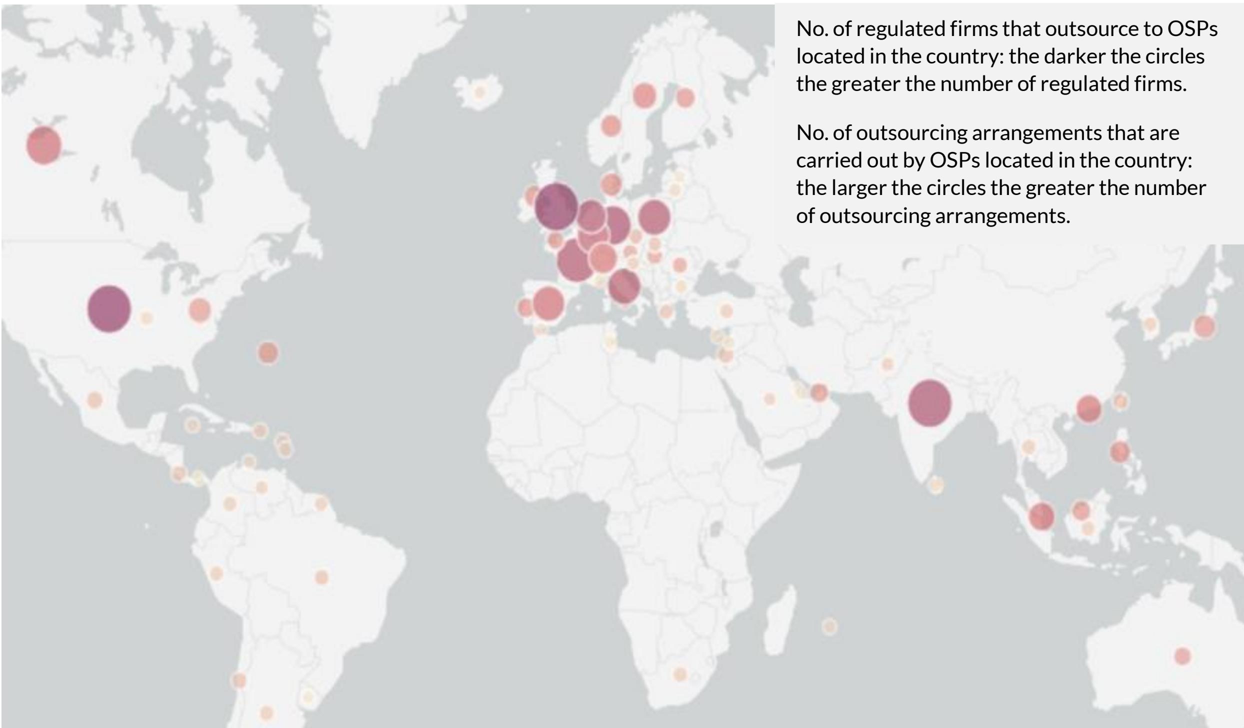
- *How are regulated firms seeking to reduce their exposure to concentration risk both from the perspective of providers and geographical locations?*
- *How are regulated firms addressing concentration risk whereby they are outsourcing to OSPs who provide services for a large proportion of their sector? Of particular interest is how regulated firms are dealing with concentration risk where there are limited numbers of providers of niche services such as CSPs?*
- *Do regulated firms have views, as to how systemic concentration risk related to outsourcing, can be effectively monitored and managed by both regulated firms in all sectors and the Central Bank?*

3. Offshoring Risk

In many cases, regulated firms choose to outsource some of their activities to another country ('offshoring') to avail of reduced costs and other benefits. Survey respondents reported offshoring to over 80 countries. Significantly, 51% of these arrangements were reported to be with OSPs located outside the EEA.

In terms of concentration, some 53% of the arrangements were said to be distributed between UK, US, India, Germany and France, the top five locations identified by the Survey. The map below highlights all of the areas where survey respondents indicated that their outsourced activities are domiciled. The colour and size of the circle intensifies according to the number of reported arrangements in each region.

3.1 Offshoring Location Distribution



It is recognised that offshoring provides many benefits to regulated firms in developing and delivering their service offering. These include, providing access to lower cost services, economies of scale and in many cases, a 24/7 service offering regardless of where customers are based. However, as with other aspects of outsourcing described in this paper, offshoring also presents challenges and risks which must be effectively managed by regulated firms throughout the lifecycle of the arrangement.

A robust methodology in the selection of the OSP and application of detailed and comprehensive service contracts and SLAs which are regularly monitored and managed thereafter, are key in establishing agreed expectations of the relationship and managing the delivery of the service under the arrangements.

3.2 Visibility and 'Supervisibility' Risk

Visibility risk is one of the key concerns associated with offshoring. While visibility risk is a concern in any outsourcing arrangement, it can be exacerbated in the case of 'offshoring'. This risk arises from the physical distance of the regulated firm from where the activity or service is being provided, complicating a regulated firm's ability to ensure effective oversight. Visibility risk can be mitigated through, inter alia; the use of robust SLAs, monitoring KPIs, regular engagement and oversight via service standard reviews, and assurance testing conducted by compliance and risk management personnel within the regulated firm (including both desk based and on-site reviews of the offshore location where appropriate).

Regulated firms should also be mindful that supervisors must be able to satisfy themselves that they have access to all information and resources required to enable them to carry out their supervisory functions. The access rights of the Central Bank do not differ depending on how a regulated firm decides to structure its business. This may include access to the physical location where regulated activities or parts of these processes and services are being carried out. As noted in Part A, Section 1.3, regulated firms must ensure that contracts for outsourced arrangements stipulate that regulated firms and the Central Bank must be given access to carry out the necessary quality assurance and supervisory work. Where the nature or location of any offshored activity creates a barrier or impedes the ability of the Central Bank to appropriately supervise the activity in any way, or where the risks associated with the offshoring of particular activities are deemed by the Central Bank to be excessive, regulated firms may be restricted from offshoring such activities.

3.3 Country Risk

Regulated firms must also consider the particular risks associated with countries to which they are planning to outsource activities and ensure that their outsourcing risk assessments pay sufficient attention to 'country risk'. In assessing country risk, regulated firms should give consideration to the following:

- **Regulatory environment** – the strength of regulatory regime in operation in the OSPs' jurisdiction;
- **Political climate risk** – risk of political agenda and/or instability and potential impacts on ability of the OSP to continue providing service;
- **Physical climate risk** – risk of offshore location being subject to extreme weather or other environmental events and potential impacts on ability of the OSP to continue providing service;
- **Cultural or language issues** – lack of understanding/ misunderstanding of expectations and/or issues arising from the outsourced arrangement;
- **Time-zones** – ability to ensure availability of the relevant OSP personnel to deal with service issues in a timely manner; and
- **Employment conditions in offshore jurisdictions** – regulated firms should pay careful attention to human rights and take into account the impact of their outsourcing on all stakeholders; this includes taking into account their social and environmental responsibilities.

Regulated firms may mitigate these risks by ensuring that contractual arrangements clearly set out that outsourced activities are required to be conducted in line with the regulatory standards and rules which apply to the regulated firm. The PwC research indicates that best practices observed in other industries includes on-site visits and the regulated firm meeting with local OSP management in advance of service commencement. This research also highlights that offshoring conditions, such as tax and labour laws, should be monitored on an ongoing basis. Offshoring should be overseen at a senior level within the regulated firm. In order to mitigate reputational risks or regulatory breaches, regulated firms should ensure that there are minimum standards in place at the OSP that are aligned to the regulated firm's risk management expectations and requirements.

In addition, issues identified as part of the country risk assessment should also be considered as part of disaster recovery (DR)/ BCP and substitutability planning.

3.4 Brexit

Given the scale of the offshoring of arrangements from Ireland to the UK (22% of all reported arrangements), it is important that regulated firms are considering and planning for the outcome of the Brexit negotiations and the potential implications for their outsourcing arrangements. Regulated firms must be forward-looking and consider 'post Brexit' issues such as possible regulatory changes in the UK, transfer of data outside of the EU and potential changes in trade, tax and employment laws etc.

The PwC research also observes that firms in other industries have established working groups to monitor and assess the possible impacts of Brexit on their operations, including on their outsourcing arrangements. Scenario planning is being undertaken to allow for the various types of trade deals between the UK and Europe that are currently envisaged as possible outcomes of Brexit negotiations. The research further highlights that where Brexit is expected to have a major impact on outsourcing operations, firms are exploring mitigation tools and options, such as the increased use of Robotic Process Automation (RPA) to replace certain outsourced functions.

4. Chain Outsourcing – Sub-Contracting

As previously outlined, the Survey data indicates that between 12% and 15% of critical or important outsourcing arrangements are further outsourced to sub-contractors. This is likely to be an underestimation largely due to, what the Central Bank perceives to be, a lack of awareness within regulated firms' management of the extent of the sub-contracting arrangements of their OSP. Chain outsourcing complicates the effective management of risk particularly when the existence of the sub-contracted party/parties is unknown. Therefore, in line with existing guidance, any contractual arrangements between regulated firms and OSPs 'should include an obligation for the OSP to inform the regulated firm of any planned sub-outsourcing, or material changes thereto, in particular where that might affect the ability of the OSP to meet its

Contractual arrangements should include the requirement for OSPs to notify the Firm of any planned sub-outsourcing. The Central Bank has observed instances where such clauses were not included in agreements.

12 – 15% of critical or important outsourcing arrangements undertaken by regulated firms surveyed, are further outsourced to sub-contractors.

responsibilities under the outsourced agreement'[34]. In the course of its supervisory engagements, the Central Bank has observed instances where such clauses were not included in agreements, with more instances noted in the context of intragroup arrangements than in arrangements with third parties.

Where a regulated firm outsources to an OSP that has sub-contracting arrangements in place, the regulated firm must ensure that the OSP oversees and manages the activities of the sub-contracted OSP to ensure the fulfilment of all services in line with the original outsourcing contract and relevant SLA.

In the context of outsourcing to offshore locations and particularly where chain outsourcing is a feature of these arrangements, regulated firms must ensure that they have appropriate visibility of any services and roles being outsourced. They must ensure that they are in a position to demonstrate and evidence to the Central Bank, that all outsourced activities are being managed and executed in a manner that is compliant with their legal and regulatory obligations.

Issues to be addressed by regulated firms

- *Has the regulated firm included offshoring risk in its outsourcing risk assessments and given consideration at a minimum to the offshoring risk factors outlined in this paper?*
- *Has the regulated firm conducted comprehensive risk assessments and scenario planning in respect of Brexit?*
- *Has the regulated firm included consideration of the risk presented by chain-outsourcing as part of their outsourcing risk assessments?*

Questions for discussion with the Central Bank

- *Given the significant volume of offshoring to the UK what preparations are regulated firms undertaking to prepare for Brexit and what related challenges are envisaged in terms of their outsourcing arrangements?*
- *What steps are regulated firms taking to ensure they have full sight of any chain outsourcing which may be occurring within their outsourcing arrangements and how are they managing risks associated with this?*
- *How are firms ensuring that contractual rights of access are the same with all parties to a chain-outsourcing arrangement, as those granted by the primary third party OSP?*

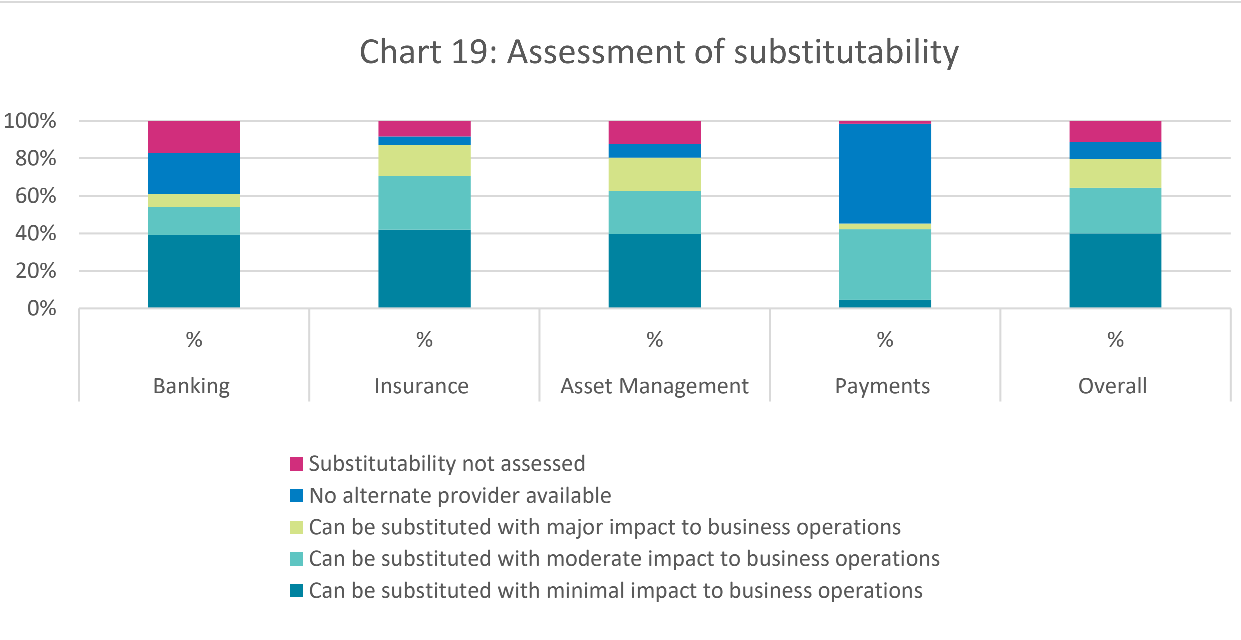
[34] EBA Draft Outsourcing Guidelines

5. Substitutability Risk

As discussed in Section 3 of Part A, regulated firms must create robust contingency planning for dealing with any scenario where the OSP, for whatever reason, gets into difficulty, or abruptly loses the capability to continue to provide or support critical business processes or systems. Any failure to do so increases the risk of significant business disruption. Regulated firms must therefore ensure that clear and viable contingency plans and exit strategies exist so that continuity of business can be maintained in any event[35].

The Central Bank has observed that in some instances, termination and transition of services either to another OSP or back in-house, has not been considered in outsourcing policies.

The EBA Draft Outsourcing Guidelines highlight that regulated firms should assess whether an OSP can be substituted and/or if it is possible to integrate the underlying service or function back into the regulated firm. Survey respondents indicated that, on aggregate, over 10% of the critical and important outsourcing arrangements reported in the Survey have not been assessed for substitutability by the respective regulated firms and that 9% of arrangements cannot be substituted at all. A total of 15% of arrangements were said to be unable to be substituted without causing major impact/disruption to business operations. The table below sets out the results of substitutability assessments by sector.



After substitutability is established, regulated firms should seek to identify alternate OSPs. Survey respondents have indicated that an alternate provider has only been identified for approximately 34% of outsourcing service agreements.

According to the aggregate survey responses, over half of existing outsourcing contracts do not have an exit strategy in place[36], while the timeframe for exit for the contracts that do have an exit strategy in place varies greatly, from less than six months to contracts where that timeframe is not determined.

[35] EBA Draft Outsourcing Guidelines

[36] 56% of respondents answered either No or N/A to the question on whether there was an exit strategy in place. For the purposes of this question, we have assumed that N/A is a No response.

It has also been noted through ongoing supervisory engagements that in many cases, termination and transition stages of services from an outsource partner to another third party or back in-house, were not considered in any outsourcing policies reviewed. A key part of these policies should be determining the substitutability of any critical service, or activity, which are currently provided under outsourcing arrangements.

The Central Bank accepts that not all services are substitutable but expects that where a regulated firm concludes that an outsourcing arrangement is not substitutable or that its substitution would lead to a material business disruption, it should assess the overall impact of the disruption of the service on its customers, its financial position and on the orderliness of its business conduct. Regulated firms should also consider what contingency arrangements can be put in place to minimise the impact of any such disruption.

Issues to be addressed by regulated firms

- *Has the regulated firm determined the substitutability of the services that they outsource?*
- *Has the regulated firm identified and engaged with an alternative provider services that they outsource and assessed the timeframe for transition?*
- *Has the regulated firm determined their ability to bring outsourced services back in house if necessary (particularly if no substitution options have been identified?*
- *Has the regulated firm considered how data will be transferred from the OSP to an alternative provider in timely and controlled manner?*

Questions for discussion with the Central Bank

- *What issues/ challenges are regulated firms encountering when assessing substitutability and exit strategies? How are these being addressed?*
- *What are the risks / challenges where there is no substitutability or it is not possible to bring the service back in house? How are these being addressed?*

Summary of issues to be addressed by regulated firms

Sensitive Data Risk

- *Has the regulated firm ensured that data protection standards applied by their OSPs are aligned to the standards required of the regulated firm?*
- *Has the regulated firm considered the need to ensure consistency of security operations between 'on premises' security and cloud security?*
- *Has the regulated firm considered the need to define standards for configuring cloud services and designing a comprehensive security architecture (identity and access management and governance, data protection and encryption, data loss prevention and security monitoring and operations)?*
- *Has the regulated firm considered the location of data when engaging the services of CSPs?*
- *Has the regulated firm considered the multiple layers in a cloud supply chain when identifying and monitoring risk?*

Concentration Risk

- *Has the regulated firm given consideration to concentration risk prior to entering into new outsourcing arrangements?*
- *Does the regulated firm seek to structure their contracts with OSPs in such a way that other OSPs are not discouraged from bidding for the service?*
- *Has the regulated firm considered concentration risk in respect of CSPs, particularly where there are a limited number of CSPs available?*
- *Has the regulated firm mapped out the concentration risk they are exposed to from chain outsourcing?*

Offshoring and Chain Outsourcing

- *Has the regulated firm included offshoring risk in its outsourcing risk assessments and given consideration at a minimum to the offshoring risk factors outlined in this paper ?*
- *Has the regulated firm conducted comprehensive risk assessments and scenario planning in respect of Brexit?*
- *Has the regulated firm included consideration of the risk presented by chain-outsourcing as part of their outsourcing risk assessment?*

Substitutability

- *Has the regulated firm determined the substitutability of the services that they outsource?*
- *Has the regulated firm identified and engaged with an alternative provider of the services that they outsource and assessed the timeframe for transition?*
- *Has the regulated firm determined their ability to bring outsourced services back in house if necessary (particularly if no substitution options have been identified?*
- *Has the regulated firm considered how data will be transferred from the OSP to an alternative provider in timely and controlled manner?*

Summary of questions for discussion with the Central Bank

Sensitive Data Risk

- *How are regulated firms ensuring that they have sufficient knowledge/ expertise within their own organisation to effectively challenge and gain assurance that their data is being managed securely by OSPs, including CSPs (how and where it is being stored, processed, used, located etc.)?*
- *What issues/ challenges are regulated firms encountering in gaining assurance that their sensitive business and customer data is being managed securely in outsourcing scenarios?*

Concentration Risk

- *How are regulated firms seeking to reduce their exposure to concentration risk both from the perspective of providers and geographical locations?*
- *How are regulated firms addressing concentration risk whereby they are outsourcing to OSPs who provide services for a large proportion of their sector? Of particular interest is how regulated firms are dealing with concentration risk where there are limited numbers of providers of niche services such as CSPs?*
- *Do regulated firms have views, as to how systemic concentration risk related to outsourcing, can be effectively monitored and managed by both regulated firms in all sectors and the Central Bank?*

Offshoring and Chain Outsourcing

- *Given the significant volume of offshoring to the UK what preparations are regulated firms undertaking to prepare for Brexit and what related challenges are envisaged in terms of their outsourcing arrangements?*
- *What steps are regulated firms taking to ensure they have full sight of any chain outsourcing which may be occurring within their outsourcing arrangements and how are they managing risks associated with this?*
- *How are firms ensuring that contractual rights of access are the same with all parties to a chain-outsourcing arrangement, as those granted by the primary third party OSP?*

Substitutability

- *What issues/ challenges are regulated firms encountering when assessing substitutability and exit strategies? How are these being addressed?*
- *What are the risks / challenges where there is no substitutability or it is not possible to bring the service back in house? How are these being addressed?*

Conclusions

The Central Bank has recently concluded a review of the outsourcing activities and related risk management practices of regulated firms operating across all sectors of the Irish financial service industry. The Central Bank's analysis of the Survey results, used to inform much of this review, has highlighted a number of gaps where regulated firms are not meeting existing supervisory expectations. A number of key risks and evolving trends relating to the outsourcing by regulated firms of important activities or services have also been identified throughout this paper.

While outsourcing risk is not new, the current and expected level of reliance of regulated firms on outsourcing arrangements to deliver their products and services across the financial services industry has brought it into sharp focus for all regulators, including the Central Bank. The implementation by all regulated firms of appropriate governance structures, with robust risk management and BCM processes, is fundamental to ensuring regulated firms can effectively monitor, manage and mitigate the risks presented by outsourcing.

Outsourcing risk is steadily moving towards the top of the risk registers for many firms across the financial services industry, a trajectory mirrored by its prominence on the list of supervisory priorities across financial sector regulators, who are more concerned now with regulated firms' capabilities and approaches to managing and mitigating outsourcing risk than ever before. In the case of the Central Bank, this is reflected in the extent and volume of mitigation actions issued to several regulated firms specifically targeting improving the management of outsourcing risk. However, as the survey results reflect, further work and improvement to the standards of outsourcing governance and risk management processes is needed on an industry-wide basis across all sectors.

This is particularly the case given the observed increase in the volume of critical services being provided by OPSs to regulated firms for the delivery of both strategic/financial targets as well the execution of robust risk management policies and processes.

It is therefore very important that regulated firms conduct appropriate outsourcing risk assessments, both initially upon consideration by the board of any outsourcing proposal, and on an ongoing basis, and ensure they have a comprehensive view of the extent of outsourcing activities. Every effort to identify and consider all the potential threats to the organisation from any outsourcing should be at the heart of any solid risk management framework. This will contribute to the adoption of proper preventative and detection measures and effective mitigation of the operational risks arising. For that reason, it is important for all regulated firms to maintain comprehensive and universal risk registers to enable the regulated firm to understand the key threats to their organisation and to ensure appropriate risk assessments and monitoring is performed regularly and routinely.

As organisations are increasingly under scrutiny for their sustainability and business continuity efforts, these are also becoming an important component of outsourcing contracts to be considered and addressed by regulated firms at inception.

Going Forward

While the Central Bank will continue its oversight of outsourcing activities by regulated entities through ongoing supervisory engagement, it is the responsibility of each regulated firm to review its current practices and make any necessary enhancements to mitigate the increasing outsourcing risk profile across all sectors. This paper has highlighted a number of key considerations that the Central Bank will build into its ongoing supervision of regulated firms, potentially including either specific or thematic follow up reviews with a focus on outsourcing risk.

This paper should be viewed as a summary of the key outsourcing issues and risks considered by the Central Bank as those requiring closest attention at this time. The Central Bank expects that all regulated firms take appropriate action to address the issues outlined in this paper and can evidence same to the Central Bank if requested. In that regard, the paper may serve as a useful guide for the management and boards of regulated firms, in considering any outsourcing arrangements currently in place and any potential new arrangements.

Part B of this paper seeks to stimulate discussion and obtain feedback from interested parties on the key risks and evolving trends associated with outsourcing. The Central Bank is continuing its examination of this topic amid increased international focus on outsourcing and against the background of an evolving financial services landscape. Responses to this Discussion Paper will inform the Central Banks

- Planning for its outsourcing conference in Q1 2019;
- Engagement in domestic, EU and international fora; and
- Ongoing consideration of its policy position in relation to outsourcing.

Finally, it is worth repeating that it is the responsibility of each individual regulated firm to know what their requirements are in relation to outsourcing risk. Therefore, while the Central Bank is keen to facilitate further open and transparent engagement, it is important to confirm that the effective management and mitigation of the operational and other risks presented by outsourcing, is ultimately the responsibility of the boards and senior management of all regulated firms across the financial services industry.

<u>Making your submission</u>

Questions for discussion are listed throughout Part B of this paper to stimulate your views. While a number of questions are posed for firms to consider internally and others are marked specifically as questions for discussion, the Central Bank also welcomes any general observations and evidence interested parties may have on the topic. It is important to note that although interested parties may not be able to respond to each question, the Central Bank would encourage partial responses on questions considered to be most relevant.

The Central Bank will make submissions received available on its website after the deadline for receiving submissions has passed. As a result, please do not include commercially sensitive material in your submission, unless you consider it to be essential. If commercially sensitive material is included, please highlight this clearly so that the Central Bank may take reasonable steps to avoid publishing that material. This may involve publishing submissions with sensitive material redacted. Despite the approach outlined, the Central Bank cannot guarantee that any information interested parties deem to be confidential will not be published. So be aware that unless any commercially sensitive information is identified, interested parties are making a submission on the basis that consent to publish-in-full is given.

This paper will be open for comment until 18 January, 2019. Submissions should be made to outsourcingfeedback@centralbank.ie.

Appendix 1 – Questions from 'Cross Sector Survey of Regulated Firms' Outsourcing Activity'

Firm Information

Ref		
	Name of Firm	[INSERT NAME HERE]
	CBI code	[INSERT CBI CODE HERE]
	Date of submission	[INSERT DATE HERE]
Q1	Total number of outsourced service arrangements in place	[INSERT TOTAL NUMBER HERE]
Q2	Total number of material and critical outsourced arrangements in place	[INSERT TOTAL NUMBER HERE]
Q3	Number of Cloud Service Providers	[INSERT TOTAL NUMBER HERE]
Q4	Does your Firm use FinTech Partnerships as part of your Strategy/Business Model?	[SELECT DROPDOWN]
Q5	Does your Firm use RegTech Companies as part of your Strategy/Business Model?	[SELECT DROPDOWN]
Q6	Is there an Outsourcing Policy with an associated Risk Management Framework in place?	[SELECT DROPDOWN]
Q7	Was the Outsourcing Policy approved by the Board?	[SELECT DROPDOWN]
Q8	Are there plans to contract with further service providers in the next 12 to 18 months?	[SELECT DROPDOWN]
Q9	Where the Firm is itself an outsourcing service provider for Irish financial services firms, please provide a brief description of the services offered	[FREE TEXT]

Outsourced Arrangements

1	Details on Outsourced Services		
Ref		*Outsourced Service 1*	*Outsourced Service 2*
1.1	Provide the category of outsourced service(s)	[SELECT DROPDOWN]	[SELECT DROPDOWN]
1.2	Brief description of outsourced service(s)	[FREE TEXT]	[FREE TEXT]
1.3	Name of service provider / material sub-contractor as set out in the outsourcing agreement	[FREE TEXT]	[FREE TEXT]
1.4	Category (Service provider or material sub-contractor)	[SELECT DROPDOWN]	[SELECT DROPDOWN]
1.5	Type of outsourcing	[SELECT DROPDOWN]	[SELECT DROPDOWN]
Commentary		[FREE TEXT]	[FREE TEXT]

Ref	2 Materiality/Concentration Assessment	*Outsourced Service 1*	*Outsourced Service 2*
2.1	**Please state whether the service outsourced is considered material or non material to your firm.**	[DROP DOWN SELECTION - "Material" or "Non-material"	[DROP DOWN SELECTION - "Material" or "Non-material"
2.2	**Please describe the criteria used in determining materiality**	[FREE TEXT]	[FREE TEXT]
2.3	**Does the outsourced/sub-contracted service provider support a critical business operation?**	[SELECT DROPDOWN]	[SELECT DROPDOWN]
2.4	**How frequently does the Firm perform materiality assessments?**	[SELECT DROPDOWN]	[SELECT DROPDOWN]
2.5	**Does the service provider / material sub-contractor store or process customer information** which in the event of any unauthorised access or disclosure, loss or theft of the information, may have a material **impact on the customer**	[SELECT DROPDOWN]	[SELECT DROPDOWN]
2.6	**Does the service provider / material sub-contractor store or process business sensitive or critical data** which in the event of any unauthorised access or disclosure, loss or theft of the information, may have a material **impact on the firm**	[SELECT DROPDOWN]	[SELECT DROPDOWN]
2.7	**Please list all the locations (city, country) where the outsourced service will be carried out**	[FREE TEXT]	[FREE TEXT]
2.8	**Please list all the locations (city, country) where customer information will be stored or processed**	[FREE TEXT]	[FREE TEXT]
2.9	**Please list all the locations (city, country) where business sensitive or critical data will be stored or processed**	[FREE TEXT]	[FREE TEXT]
Commentary		[FREE TEXT]	[FREE TEXT]

Ref	3 Contractual Arrangements	*Outsourced Service 1*	*Outsourced Service 2*
3.1	**Is there a written contract in place relating to the outsourced service(s)?**	[SELECT DROPDOWN]	[SELECT DROPDOWN]
3.2	**Is there a Service Leval Agreement ("SLA") in place relating to the outsourced service(s)?**	[SELECT DROPDOWN]	[SELECT DROPDOWN]
3.3	**When was the Outsourcing Agreement / Service Level Agreement last reviewed?**	[SELECT DROPDOWN]	[SELECT DROPDOWN]
3.4	**Does your Outsourcing Agreement / Service Level Agreement contain provisions to manage the use of sub-contractors?**	[SELECT DROPDOWN]	[SELECT DROPDOWN]
Commentary		[FREE TEXT]	[FREE TEXT]

4	**Contingency Planning**		
Ref		*Outsourced Service 1*	*Outsourced Service 2*
4.1	Is there service provider substitutability established	[SELECT DROPDOWN]	[SELECT DROPDOWN]
4.2	Has an alternate service provider been identified	[SELECT DROPDOWN]	[SELECT DROPDOWN]
4.3	If answer "yes" to Q 4.2 above, please provide name(s) of alternate service provider	[FREE TEXT]	[FREE TEXT]
4.4	Is there a documented "Exit Strategy" in place?	[SELECT DROPDOWN]	[SELECT DROPDOWN]
4.5	What is the estimated timeframe for transfer of service in the event of exit from existing contract?	[FREE TEXT]	[FREE TEXT]
Commentary		[FREE TEXT]	[FREE TEXT]

5	**Oversight and Assurance**		
Ref		*Outsourced Service 1*	*Outsourced Service 2*
5.1	How frequently does the Firm conduct due diligence on the service provider/material sub-contractor after initiation of the contract?	[SELECT DROPDOWN]	[SELECT DROPDOWN]
5.2	How frequently is an independent review/audit conducted on the outsourced service provider/material sub-contractor?	[SELECT DROPDOWN]	[SELECT DROPDOWN]
5.3	When was an independent review/audit last conducted on the service provider/ material sub-contractor? (input as "mm/yyyy")	[INSERT DATE]	[INSERT DATE]
5.4	Who conducted the last independent review/ audit?	[SELECT DROPDOWN]	[SELECT DROPDOWN]
5.5	What was the objective and nature of the last independent review/audit conducted?	[FREE TEXT]	[FREE TEXT]
5.6	Has any "on-site" inspection or review of controls (excluding Regulatory Inspections) been conducted on the service provider/material sub-contractor?	[SELECT DROPDOWN]	[SELECT DROPDOWN]
5.7	Does the Firm perform annual testing and/or review of the Business Continuity Plan ("BCP") of the service provider/material sub-contractor?	[SELECT DROPDOWN]	[SELECT DROPDOWN]
5.8	Did the material and/or critical service provider/material sub-contractor meet all of the objectives of the BCP test successfully?	[SELECT DROPDOWN]	[SELECT DROPDOWN]
5.9	Where Anti Money Laundering ('AML')/Counter Financing of Terrorism ('CFT')/Financial Sanction ('FS') service(s) is outsourced is sampling of customer/client records undertaken as part of the "onsite inspection"?	[SELECT DROPDOWN]	[SELECT DROPDOWN]
5.10	Where sampling is undertaken, what proportion (as a % of total) of customer records are tested?	[INSERT %]	[INSERT %]
Commentary		[FREE TEXT]	[FREE TEXT]

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