CP 138 - Cross-Industry Guidance on Outsourcing

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Date: Deadline 26th July 2021

Ref: Consultation Paper 138 Cross-Industry Guidance on Outsourcing (CP 138)

Dear Sir/Madam,

Thank you for the opportunity to engage with you on the topic of Cross Industry Guidance on Outsourcing through your recent Consultation Paper 138 ('the CP').

The Irish league of Credit Unions ("ILCU") is the largest credit union representative body on the island of Ireland. It was founded to provide representation, leadership, co-operation, support and development for credit unions in both the Republic of Ireland ("ROI") and Northern Ireland ("NI"). Credit Unions affiliated to the ILCU elect the Directors of the ILCU and ultimately determine what the ILCU delivers. The ILCU responds directly to the needs of the affiliated credit unions. As an advocate of the credit union ethos of mutuality, volunteerism, self-help and not for profit philosophy, the ILCU has a vision to influence and inspire the credit union movement to achieve all its objectives, social, economic and cultural while always respecting the individual's rights and dignity. There are approximately 211 credit unions affiliated to the ILCU. Any and all references to credit unions in this document refer to credit unions affiliated to the ILCU.

Having consulted with our members, and reviewed the global position[1] from a credit unions perspective, we are pleased to set out our view on the proposals on this important topic.

If you have any questions or would like more detail, please feel free to contact us.

Yours sincerely,

Ed Farrell

Ed Farrell,
CEO, ILCU.

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[1] World Council response to the Financial Stability Board, regarding Regulatory and Supervisory Issues Relating to Outsourcing and Third-Party Relationships dated January 08, 2021
ABCUL response to Financial Conduct Authority, regarding Building Operational Resilience: Impact tolerances for important business services and feedback to DP18/04 dated October 01, 2020
UK Finance response to PRA Consultation Paper on Outsourcing and third party risk management (CP30/19) dated September 30, 2020

ILCU Submission regarding CP 138 - Consultation Paper for Cross Industry Guidance on Outsourcing

Consultation Questions	
Are there are any aspects of the Guidance that are unclear? If so, please advise what these are and provide suggestions on the additional clarity required.	While the ILCU is broadly supportive of the Cross Industry Guidance on Outsourcing (hereinafter “Guidelines”) for financial institutions, it is important to acknowledge that a further regulatory requirement may signify a considerable challenge for the credit union sector. With respect to Part A - Section 4 of the Guidance *"...Certain aspects of this Guidance may not be appropriate to all regulated firms, due to their nature, scale and complexity. The Central Bank acknowledges that it may not be appropriate for certain smaller, less complex regulated firms to adopt, in full, all measures set out in the Guidance..."* ***The Guidance should state which parts of the guidance may not be appropriate particularly as it relates to the credit union sector.*** *"...The test for proportionality should always be underpinned by the regulated firm’s outsourcing risk assessment and resulting controls. The extent of measures applied should also be informed by the regulated firm’s assessment of whether the outsourced service or activity is deemed critical or important (as set out in section 2.1 below)..."* ***Proportional and risk-based regulation and supervision is the most effective way of regulating smaller institutions such as credit unions. It would be helpful if there were specific guidelines on proportionality that consider the size, risk and complexity of each entity which would allow credit unions to implement and monitor risk without subjecting them to the complex regulations that are not applicable to the individual risk of that entity, and in effect strips resources and capital from the underserved banking community who benefit from the much needed services credit unions provide.*** With respect to Part B - Section 9 of the Guidance; Exit Strategies & Appendix 3 *“…Have a clearly defined and documented exit strategy in place (in particular for their critical or important outsourcing arrangements), which is viable, appropriately planned, documented and regularly tested and takes into account at least the circumstances detailed in Part B Section 9.1…”* ***The testing of exit plans is an area of concern to our members. They are supportive of the need for credibility around their contingency arrangements and cognisant of the CBI findings as documented in this regard in the IT Risk in Credit Unions - Thematic Review Findings (January 2018) but there are significant limitations around the extent to which***

	many plans can be tested. Clarity of the outcome sought and some 'good practice' examples would be welcomed. Please indicate what supporting evidence needs to be recorded in the Register/Database and CBI Regulatory Return. With respect to Part B - Section 4.2 of the Guidance; Strategy and Policy for Outsourcing *"…In the context of information and communications technology (ICT) that regulated firms' strategy considers what services and ICT operations they are retaining within the organisation and the different risks associated with outsourcing, particularly in the case of cloud based offerings. A regulated firm's choice should be aligned not only to its operational needs and operational risk appetite but also its capability to oversee and manage the cloud outsourcing arrangements once entered into; …"* ***Some Credit unions do not have in-house expertise to oversee and manage these cloud outsourcing arrangements. While acknowledging the CBI findings as documented in this regard in the IT Risk in Credit Unions - Thematic Review Findings (January 2018), can CBI clarify how they expect credit unions address this requirement?*** With respect to Part B - Section 8.3 of the Guidance: Use of Third Party Certifications and Pooled Audits *"…Regulated firms assess and document the circumstances in which third party certifications and pooled audits are deemed to provide appropriate levels of assurance, in line with their outsourcing policy and risk assessment…"* ***Could the CBI give some examples on what 'circumstances' would warrant / justify / lead to an expectation of the use of third party certifications and pooled audits. Credit unions use assurance reports based on pooled testing of the system arranged by the IT user groups which would be an important and efficient aspect of the risk controls. Credit unions would be keen to ensure that such assurance reports would be considered appropriate under the guidance.***
What, if any, are the other areas/topics that should be covered in the Guidance (specify sections) or in future versions of the Guidance?	With respect to Part B – Section 5.1 Sub-Outsourcing Risk *"…In the case of sub-outsourcing of critical or important functions regulated firms should themselves apply an appropriate level of monitoring of the sub-outsourced service providers in line with their outsourcing risk assessment;…"* ***We would like clarification on what the CBI deems an 'appropriate level of monitoring' of fourth parties, or whether reliance can be placed upon the due diligence of the contracted third party. Additionally, our members request acknowledgement by the CBI that mandating oversight of fourth parties will likely result in this requirement becoming overly burdensome when combined with normal due diligence processes undertaken by the contracted third party and have a significant impact on the costs and associated timelines of compliance.*** ***Individual credit unions are significantly smaller than their banking counterparts in terms of asset values and while they are very well reserved (with reserves of over 10% of total assets) they do not have the level of resources (in value terms)***

	that are available to larger banks. Their risks often arise from their lack of bargaining power due to their small size or perceived small volume of business and are often unable to negotiate favourable contractual clauses. These contractual risks often pose risk to the credit unions. They often are forced to accept these terms or forego the desired service, which can have compliance implications. Regulatory influence could be very effective to the credit union sector who often find themselves dependent on a limited number of outsourced / sub-outsourced providers which in turn has a concentration risk. With respect to Part B – Section 5.2 Sensitive Data Risk *"…iii. consider and document data issues that might arise in the event of termination, insolvency and or recovery / resolution events;…"* ***We suggest expanding this section with respect to the extent of data relating to the firms and its member/customers, where applicable, that would be required to be retained by the OSP in the event of an exit to be documented in the data management strategy. Examples include the type of data to be retained, such as to assist with complaint resolution, the period of data retention and safeguards required for the data.***
What, if any, are the significant issues /or concerns or unintended consequences that might arise due to the provisions of the Guidance?	With respect to Part B – Section 5.4 of the Guidance: Concentration Risk "…Evaluate elements of concentration risk and evidence such in the risk assessments and due diligence review when outsourcing critical or important functions. These considerations should include: i. Single firm concentration of multiple services at same OSP or intragroup service provider; ii. Lack of substitutability issue arising from single service provider in the marketplace; iii. Multiple number of regulated firms outsourcing to same OSP either on a sectoral or cross sectoral basis;…" ***It would be helpful if there was further clarification in relation to Concentration Risk, particularly as it applies in the context of IT providers to credit unions, more specific information required on Substitutability, particularly when there are a limited number of IT/ Specialist providers serving this market.***

General Feedback
COVID-19 has presented numerous challenges for credit unions including the challenge of providing our members with access to remote financial services. The pandemic has created an urgency to make strides towards greater digital transformation, particularly for those financial institutions that still lack online and mobile transaction services. There has been a decline in branch visits and cash transactions for credit unions. This trend is not likely to change once the pandemic subsides. This need for digitisation for credit unions will inherently mean the reliance on third party relationships to assist in the transformation. We do acknowledge that the volume and complexity of these relationships will continue to increase over time bringing with it increased risk, supply-chain risk, IT risk, privacy risks, reputational risks and others. The key, however, is understanding that the transformation is likely mandatory if a business or financial institution intends to survive as a viable entity. With that in mind, drafting regulations that balance the ability to have access to third party providers in an affordable manner so long as the proportional risks are managed adequately by the credit union is imperative.