

CONSULTATION PAPER

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Public Consultation : Guidelines on Outsourcing

MAS

Monetary Authority of Singapore

INVITATION TO COMMENT

MAS invites interested parties to provide their views and comments on the Guidelines on Outsourcing. Written comments should be submitted by 12 April 2004 to:

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Please note that all submissions received may be made public unless confidentiality is specifically requested for the whole or part of the submission.

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1 INTRODUCTION

1.1 While outsourcing can bring cost and other competitive advantages, it increases the risk profile of an institution, particularly its strategic, reputational, operational and compliance risks. Failure of a service provider in providing the service, breaches in security, or non-compliance with legal and regulatory requirements by either the service provider or an institution can lead to financial losses for the institution and contagion risks within the financial system. It is therefore important that an institution adopts sound and responsive risk management practices for effective oversight, due diligence and management of risks arising from outsourcing prior to entering into such arrangements, and on an ongoing basis.

1.2 The Guidelines on Outsourcing (“these guidelines”) set out MAS’ expectations of every institution that has entered into outsourcing arrangements or is planning to outsource one or more of its business activities to a service provider. While these guidelines are intended to provide direction and guidance on outsourcing, the ultimate responsibility and accountability for outsourcing rests with the institution, its board of directors (“the board”) and management.

2 APPLICATION OF GUIDELINES

2.1 The Annex provides examples of outsourcing to which the guidelines are applicable, and arrangements that are generally not intended to be subject to these guidelines. Subject to the Annex, the guidelines are applicable to outsourcing arrangements entered into by any institution with a service provider located in Singapore or elsewhere. The service provider may be a member of the group to which the institution belongs, for example, its Head Office (HO), parent institution, another branch or related company, or an unrelated party.

2.2 It is recognised that the risks to an institution in outsourcing will vary depending on the nature, scope and complexity of the outsourcing arrangement and risk profile of the institution. MAS is particularly interested in material outsourcing which, if disrupted, has the potential to significantly impact an institution’s business operations, reputation or profitability and which can have systemic implications. Paragraph 5 provides factors to help an institution consider what is material outsourcing. Where an outsourcing arrangement is material, MAS expects an institution to apply all the Risk Management Practices in paragraph 6 of these guidelines to the arrangement.

2.3 In supervising an institution, MAS will review the extent to which the institution applies the guidelines to assess the quality of its risk management systems. MAS expects the institution to have policies and procedures to assess the materiality of arrangements and establish risk management practices commensurate with the materiality of, and level of risks posed to the institution by the outsourcing. An institution should notify MAS of material outsourcing arrangements that it is planning to enter into or has entered into. MAS should also be notified of potential adverse developments relating to an outsourcing arrangement that could significantly affect the institution. Supervisory actions taken by MAS will depend on the potential impact on the institution and the financial system.

2.4 MAS may require an institution to modify, make alternative arrangements or re-integrate the activity into the institution, as necessary, where:

- a) an institution fails or is unable to address the risks and deficiencies arising in its outsourcing in a satisfactory and timely manner;
- b) adverse developments arise in outsourcing which could significantly affect an institution; or
- c) MAS' supervisory powers and ability to carry out its supervisory functions are hindered.

2.5 An institution is expected to also consider the impact on its consolidated operations, outsourcing arrangements that are entered into or planned by its branches and corporations under its control, including those located outside Singapore. MAS expects an institution to subject its branches and corporations under its control to these guidelines.

2.6 Self Assessment and Rectification

An institution should conduct a self-assessment of its existing outsourcing arrangements against these guidelines, and where there are deficiencies, to rectify them as soon as practicable.

3 DEFINITIONS

3.1 In these guidelines, unless the context otherwise requires:

“business activities” is to be read interchangeably with business and operational functions and processes.

“institution” means any bank licensed under the Banking Act (Cap 19), any merchant bank approved under the Monetary Authority of Singapore Act (Cap 186), any finance company licensed under the Finance Companies Act (Cap. 108), any insurance company registered under the Insurance Act (Cap. 142), any exchange holding company or securities exchange or futures exchange or clearing house or Capital Markets Services (CMS) licensee approved, licensed or registered under the Securities and Futures Act (Cap. 289) (SFA), or any public company approved under section 289 of the SFA to act as a trustee for collective investment schemes authorised under section 286 of the SFA.

“outsourcing” means an arrangement whereby a third party (the “service provider”) undertakes to provide an institution with a service that may already or can conceivably be performed by the institution itself.

“material outsourcing” means an outsourcing arrangement which, if disrupted, has the potential to significantly impact an institution’s business operations, reputation or profitability.

4 LEGAL AND REGULATORY OBLIGATIONS

4.1 Every institution is reminded that outsourcing does not diminish its obligations, and those of its board and senior management, to comply with the relevant laws and regulations in Singapore. It is for an institution, when performing its due diligence in relation to outsourcing, to consider all relevant laws, regulations, guidelines and conditions of approval, licensing or registration. Risk management practices should therefore include steps to ensure legal and regulatory requirements are met. It is not the intention of these guidelines to either supersede legal and regulatory requirements or provide institutions with a list of such requirements. MAS’ supervisory powers over institutions and ability to carry out supervisory functions should also not be hindered by outsourcing, whether the service provider is located within Singapore or elsewhere.

4.2 Every institution should ensure, inter alia, that it conducts its business with integrity and competence. Hence, an institution should not engage in any outsourcing that would result in its internal control systems,

business conduct or reputation being compromised or weakened after the activity has been outsourced. An institution should only select service providers that employ high standards of care, and have the capabilities, to meet compliance requirements as if the activities were not outsourced and conducted within the institution.

4.3 Notwithstanding these guidelines, MAS Notice to Banks 634 and MAS Notice to Merchant Banks 1108 “Banking Secrecy – Conditions for Outsourcing” apply to banks and merchant banks, respectively, when banks utilise the outsourcing exception provided for in Paragraph 3, Part II, Third Schedule of the Banking Act or when merchant banks utilise the outsourcing exception provided for in Paragraph 3, Part II, Third Schedule of the Banking Regulations 2001.

5 MATERIAL OUTSOURCING

5.1 An institution may enter into outsourcing arrangements that, if disrupted, have the potential to significantly impact its business operations, reputation or profitability. Such arrangements are considered material outsourcing. An institution should assess if an outsourcing arrangement that is in existence or being planned, is material. In assessing the materiality of such arrangements, MAS recognises that qualitative judgment is involved and the circumstances faced by individual institutions may vary. Factors that an institution should consider include, among others:-

- Importance of the business activity to be outsourced, for example, in terms of contribution to income and profit;
- Potential impact of the outsourcing on earnings, solvency, liquidity, funding and capital and risk profile;
- Impact on the institution’s reputation and brand value, and ability to achieve its business objectives, strategy and plans, should the service provider fail to perform the service;
- Cost of the outsourcing as a proportion of total operating costs of the institution;
- Aggregate exposure to a particular service provider in cases where the institution outsources various functions to the same service provider; and

- Ability to maintain appropriate internal controls and meet regulatory requirements, if there were operational problems faced by the service provider.

Outsourcing of all or substantially all risk management and internal control functions including compliance, internal audit and financial accounting, whether to a service provider within a group or to an unrelated party, is to be considered material.

5.2 Any institution which has entered into or is planning material outsourcing, or is planning to vary any such outsourcing arrangements, should notify MAS of such arrangements. In line with MAS' risk-focused supervisory approach, an institution should expect to be engaged by MAS on these plans and arrangements as proportionate to the level of risks of the outsourcing. MAS expects an institution to demonstrate that it has established a robust risk management framework (for identification, measurement, monitoring and control of risks, and risk mitigating strategies), undertaken a rigorous and analytical assessment of the key risks and its capacity to apply risk mitigation strategies as commensurate with the materiality of and level of risk in the operations, and addressed all legal and regulatory requirements. This also applies to any arrangement with the institution's HO, its parent institution, another branch or its related company. An institution is expected to ensure that the home or host regulator or both, of the institution or the service provider, is aware of the outsourcing arrangement. MAS may also consult and require letters of undertakings from these parties, as appropriate, to meet its supervisory objectives. The supervisory actions to be taken by MAS will depend on the potential impact on the institution and the financial system.

5.3 An institution should undertake periodic reviews of its outsourcing arrangements to identify new material outsourcing risks as they arise. An arrangement which was previously not material may subsequently become material from incremental activities outsourced to the same service provider or an increase in volume or nature of the activity outsourced to the service provider. Material outsourcing risks may also arise when the service provider in a material outsourcing plans to sub-contract¹ the service or makes significant changes to its sub-contracting arrangements. An institution should consider materiality at both the institution and on a consolidated basis, i.e. together with the institution's branches and corporations under its control.

¹ Sub-contracting is where the service provider of an outsourced activity further contracts out that activity or a sub-component of that activity to a third party.

6 RISK MANAGEMENT PRACTICES

6.1 Role of the Board and Senior Management

6.1.1 The board and senior management of an institution are ultimately responsible for the effective management of the risks arising from outsourcing arrangements entered into by the institution. They need to fully understand the risks associated with the outsourcing as they continue to retain accountability and responsibility for managing and controlling the operational risks of their institution. While an institution can delegate their day-to-day operational duties to the service provider through such arrangements, the effective due diligence, oversight, management of outsourcing and accountability continue to rest with the institution, its board and management.

6.1.2 The board should ensure that there are appropriate policies and practices that suitably address the specific risks posed by outsourcing. The board, or a committee delegated by it, is responsible for:-

- Approving a framework to evaluate the risks and materiality of all existing and prospective outsourcing and the policies that apply to such arrangements;
- Laying down the appropriate approval authority for all outsourcing depending on the significance of their risk and materiality;
- Assessing management competencies responsible for developing sound and prudent outsourcing risk management policies and procedures as commensurate with the nature, scope and complexity of the outsourcing arrangements;
- Undertaking regular review of outsourcing strategies and arrangements for their continued relevance, and safety and soundness; and
- Reviewing a list of all material outsourcing and relevant reports on outsourcing.

In addition, the board should be actively involved in decisions to outsource business activities of a material nature, and should approve such arrangements.

6.1.3 Senior management is responsible for:-

- Evaluating the materiality and risks of all existing and prospective outsourcing, based on the framework approved by the board;
- Developing and implementing sound and prudent outsourcing policies and procedures commensurate with the nature, scope and complexity of the outsourcing;
- Reviewing periodically the effectiveness of policies and procedures;
- Communicating information pertaining to material outsourcing risks to the board in a timely manner;
- Ensuring that contingency plans, based on realistic and probable disruptive scenarios, are in place and tested; and
- Ensuring that there is independent review and audit for compliance with set policies.

6.1.4 For a foreign-incorporated institution operating in Singapore, responsibility for the functions in paragraph 6.1.3 lies with the management responsible for the institution's operations in Singapore. In cases where a regional or HO management team is responsible for overseeing the group's outsourcing, these duties may be performed by the regional or HO management team. However, local management should take necessary steps to enable it to discharge its obligations to comply with the relevant laws and regulations in Singapore, including expectations under these guidelines. Local management cannot abrogate its governance responsibilities to run the institution in a prudent and professional manner.

6.2 **Evaluation of Risks**

6.2.1 An institution should develop a framework to evaluate the risks of outsourcing. The board and senior management of an institution need to be fully aware of and understand the risks so that their institution does not enter into arrangements that will result in the internal control systems, business conduct or reputation of the institution being compromised or weakened after the activity is outsourced. Such assessments should be performed at the highest level of management and re-performed

periodically, and considered as part of strategic planning. The framework for risk evaluation should include the following:-

- Identification of the role of outsourcing in the overall business strategy and objectives of the institution, and its interaction with corporate strategic goals;
- Conduct of comprehensive due diligence on the nature, scope and complexity of the outsourcing to identify the key risks and risk mitigation strategies;
- Analysis of the impact of the arrangement on the overall risk profile of the institution, taking into consideration the adequacy of the internal expertise and resources needed to mitigate the risks identified; and
- Risk-return analysis of the potential benefits of outsourcing against the vulnerabilities that may arise, ranging from the short-term impact of temporary service disruptions to long-term impact on business continuity preparedness, and whether for strategic and internal control reasons, the arrangement should not be entered into.

6.3 Capability of Service Providers

6.3.1 In considering or renewing an outsourcing arrangement, appropriate due diligence should be performed to assess the capability of the service provider to comply with obligations in the outsourcing agreement. Due diligence should take into consideration qualitative and quantitative, financial, operational and reputation factors. Institutions should emphasise compatibility and performance in its selection process. Where possible, the institution should obtain independent reviews and market feedback on the service provider to supplement its own findings.

6.3.2 Due diligence should involve an evaluation of all available information about the service provider, including but not limited to:-

- Experience and competence to implement and support the proposed activity over the contracted period;
- Financial strength and resources (the due diligence should be similar to a credit assessment of the viability of the service provider based on reviews of business strategy and goals, audited financial statements, the strength of commitment of

significant equity sponsors and ability to service commitments even under adverse conditions);

- Business reputation and culture, compliance, complaints and outstanding or potential litigation;
- Security and internal control, audit coverage, reporting and monitoring environment;
- Business continuity management (standards should be commensurate with that expected of the institution as set out in MAS' Business Continuity Management Guidelines);
- Reliance on and success in dealing with sub-contractors;
- Insurance coverage; and
- External factors (such as the political, economic, social and legal environment of the jurisdiction in which the service provider operates, and other events) that may impact service performance.

6.3.3 Due diligence undertaken during the selection process should be documented and re-performed periodically as appropriate given the level of risks of the outsourcing.

6.4 Outsourcing Agreement

6.4.1 Contractual terms and conditions governing the relationships, functions, obligations and responsibilities of all the contracting parties should be carefully and properly defined in written agreements and vetted by a competent authority on their legal effect and enforceability. Every agreement should address the risks and risk mitigation strategies identified at the risk evaluation and due diligence stages. The agreement should be sufficiently flexible to allow the institution to retain an appropriate level of control over the outsourcing and the right to intervene with appropriate measures to meet legal and regulatory obligations.

6.4.2 Outsourcing agreements should contain, amongst others, provisions pertaining to:-

- a) The scope of the outsourcing service;

- b) Performance standards defined in terms of service levels and performance targets; service availability, reliability, stability and upgrade;
- c) Confidentiality and security [see paragraph 6.5];
- d) Business continuity management [see paragraph 6.6];
- e) Monitoring and control [see paragraph 6.7];
- f) Audit and inspection [see paragraph 6.8];
- g) Dispute resolution
Agreements should specify the resolution process, events of default, and the indemnities, remedies and recourse of the respective parties in the agreements;
- h) Default termination and early exit
An institution should have the right to terminate the agreement in the event of default, including circumstances when the service provider undergoes a change in ownership, becomes insolvent, goes into liquidation, receivership or judicial management, whether in Singapore or elsewhere; there has been a breach of security, confidentiality or demonstrable deterioration in the ability of the service provider to perform the service as contracted; and
- i) Sub-contracting
Agreements should contain rules and limitations on sub-contracting. Regard should be made to confidentiality obligations on customer information to which institutions are subject, where applicable. Prior approval should be obtained from the institution for any sub-contracting of a material nature so as to ensure that the same standards that apply to the service provider should apply to sub-contractors.

6.4.3 Agreements should be tailored to address additional issues arising from country risks and potential obstacles in exercising oversight and management of the arrangements when outsourcing to a service provider outside Singapore. Please see paragraph 6.9.

6.5 Confidentiality and Security

6.5.1 Given that public confidence and customer trust in financial institutions are a cornerstone in the stability and reputation of the financial industry, it is vital that an institution seeks to preserve and protect the security and confidentiality of customer information in the custody or possession of service providers. An institution should ensure that service providers implement security policies, procedures and controls that are at least as stringent as its own.

6.5.2 At a minimum, an institution should:-

- Specify requirements for confidentiality and security in the outsourcing agreement. An institution should be proactive in specifying requirements and not cede its responsibility to the service provider;
- Address, agree and document the respective responsibilities of the various parties in the outsourcing to ensure the adequacy and effectiveness of security policies and practices, including the right of each party to change security requirements as circumstances require. It should also address the issue of the party liable for losses in the event of a breach of security and the service provider's obligation to inform the institution, in order for the institution to meet MAS' requirement to be notified of such events;
- Provide written notice to the service provider highlighting the institution's obligations on confidentiality under common law and other relevant laws and regulations and incorporate confidentiality clauses in outsourcing agreements to address issues of access and disclosure of customer information provided to the service provider. Customer information disclosed by the institution to the service provider should be used strictly for the purpose for which they were disclosed; access to customer information by staff of the service provider should be appropriately limited to those who need the information in order to perform the outsourced function; and further disclosure of the institution's customer information to any other party should be prohibited unless with the prior approval of the institution;
- Disclose customer information to the service provider only on a need-to-know basis and ensure that the amount of information

disclosed is commensurate with the requirements of the situation;

- Ensure the service provider is able to isolate and clearly identify the institution's customer information, documents, records and assets to protect the confidentiality of the information. An institution should also ensure that the service provider takes technical, personnel and organisational measures in order to maintain the confidentiality of customer information between its various customers; and
- Review and monitor the security practices and control processes of the service provider on a regular basis, including commissioning or obtaining periodic expert reports on security adequacy and compliance in respect of the operations of the service provider, and requiring the service provider to disclose security breaches resulting in unauthorised access that affect the institution or its customers.

6.5.3 MAS expects every institution to have appropriate confidentiality and security protection in place as commensurate with the nature, scope and complexity of the outsourcing. An institution should also read these guidelines in conjunction with MAS' Internet Banking Technology Risk Management Guidelines.

6.6 Business Continuity Management

6.6.1 An institution should require its service providers to develop and establish a framework that defines their roles and responsibilities for documenting, maintaining and testing business continuity management (BCM) plans and recovery procedures, that are at least as robust as its own. There should also be reviews and agreement with service providers on the adequacy of BCM plans as part of the service provider selection, and on an on-going basis.

6.6.2 Parties and personnel involved in an outsourcing arrangement should receive regular training in activating BCM plans and executing the recovery procedures. In anticipation of such a situation, an institution needs to ensure that the service provider develops and periodically tests its BCM plans. An institution should also require the service provider to notify it of any significant changes in its BCM plans. Ideally, there should be regular joint BCM testing and recovery exercises between the institution and its service providers.

6.6.3 An institution should put in place BCM plans based on probable worst-case scenarios to mitigate the risk of unexpected termination of the outsourcing agreement or liquidation of the service provider. An institution should retain an appropriate level of control over its outsourcing and the right to intervene with appropriate measures to continue its business operations without incurring prohibitive expense. The identification of viable alternatives for resuming operations is also essential to mitigate interdependency risk.

6.6.4 Outsourcing often leads to the sharing of facilities operated by the service provider. An institution should ensure that service providers are able to isolate the institution's information, documents and records, and other assets. This is to ensure that in adverse conditions, all documents, records of transactions and information given to the service provider, and assets of the institution, can be either removed from the possession of the service provider in order to continue its business operations, or deleted, destroyed or rendered unusable.

6.6.5 The robustness of the BCM framework should be commensurate with the materiality of, and level of risks in, the outsourcing. It should take into consideration the principles for sound BCM recommended in the Business Continuity Management Guidelines issued by MAS.

6.7 Monitoring and Control of Outsourced Activities

6.7.1 An institution needs to establish a management structure to monitor and control outsourcing. Such a structure will vary depending on the nature, scope and complexity of the outsourced activity. As outsourcing relationships and interdependencies increase in materiality and complexity, a more rigorous risk management approach should be adopted. An institution also has to be more proactive in its relationship with the service provider e.g. through frequent meetings, to ensure that performance levels are upheld. An institution should ensure that outsourcing agreements with service providers contain provisions to address their monitoring and control of outsourced activities.

6.7.2 The structure for effective monitoring and control of material outsourcing could comprise the following:-

- A central record of all material outsourcing that is readily accessible for review by the board and senior management of the institution. Information maintained in the record should include the name(s) and location(s) of service provider(s), the

value and expiry or renewal dates of the contract, and reviews on the performance of the outsourced arrangement. The record should be updated promptly and form part of the corporate governance reviews undertaken by the board and senior management of the institution;

- Multi-disciplinary project management groups with members from functions including legal, compliance and finance, to ensure that other than technical issues, legal and regulatory requirements are also met. Sufficient resources, in terms of both time and manpower, should be allocated to the management groups to enable staff to adequately plan and oversee the entire outsourcing effort;
- Management control groups to monitor and control the outsourced service on an ongoing basis. There should be policies and procedures to monitor service delivery, performance reliability and processing capacity of the service provider for the purpose of gauging ongoing compliance with agreed service levels and the viability of its operations. Such monitoring could be through the review of reports by auditors of the service provider or audits commissioned by the institution;
- Reporting procedures to ensure adverse developments arising in any outsourced activity are brought to the attention of the board, senior management or both, of the institution and that of the service provider on a timely basis. Actions should be taken by an institution to review the outsourcing relationship for modification or termination of the agreement; and
- Regular audits either by the internal auditors or external auditors or agents appointed by the institution, of the service provider, and of its own internal outsourcing risk management processes. The audits should assess the adequacy of the risk management practices adopted in overseeing and managing the outsourcing arrangement, the institution's compliance with its risk management framework and the requirements of these guidelines. As a practice, institutions should conduct pre- and post implementation reviews. Any deterioration, deficiency or breach should be reported to board, senior management or both, of the institution, as appropriate, and rectified. The scope of the reviews should be adjusted depending on the nature of the outsourcing arrangement. Please also see paragraph 6.8.

6.7.3 MAS should be informed if there are adverse developments or non-compliance with legal and regulatory requirements in an outsourcing arrangement.

6.8 Audit and Inspection

6.8.1 Outsourcing should not impede or interfere with the ability of the institution to effectively oversee and manage its activities or impede MAS in carrying out its supervisory functions and objectives. Every institution should therefore ensure that outsourcing agreements include clauses to:-

- Provide the institution with the right to conduct audits, whether by its internal or external auditors, or by agents appointed to act on its behalf, on the service provider; and to obtain copies of any audit or review reports and findings made on the service provider in conjunction with the services performed for the institution; and
- Allow MAS or any agent appointed by MAS to act on its behalf to access the institution's documents, records of transactions, and information given to, stored or processed by the service provider.

6.8.2 An institution should ensure that an independent report on the service provider is prepared annually, highlighting any deterioration, deficiency or breach in service delivery, performance reliability, processing capacity, and security and confidentiality at the service provider, for the purpose of gauging ongoing compliance with the outsourcing agreement and viability of the operations of the service provider. The report may be prepared by internal or external auditors, or agents appointed by the institution, or external auditors or other third parties engaged by the service provider. The institution should ensure that the persons appointed are qualified to perform the review, that the scope of the review satisfies its own control objectives, and that any deterioration, deficiency or breach reported is rectified. The institution is expected to understand the nature, scope and complexity of the engagement and the level of assurance that can be derived from the work. Audit reports should not be regarded as a substitute for monitoring and control procedures that an institution should implement over the service provider.

6.8.3 Copies of audit reports should be submitted by the institution to MAS as is the case for reports prepared by its internal or external auditors on activities conducted within the institution.

6.9 Outsourcing Outside Singapore

6.9.1 The engagement of service providers in a foreign country exposes an institution to country risk - economic, social and political conditions and events in a foreign country that may adversely affect the institution. Such conditions and events could prevent the service provider from carrying out the terms of its agreement with the institution. To manage country risk, an institution should take into account and closely monitor government policies and political, social, economic and legal conditions in countries where the service provider is based, during the risk assessment process and on a continuous basis, and establish sound procedures for dealing with country risk problems. This includes having appropriate contingency and exit strategies. In principle, arrangements should only be entered into with parties operating in jurisdictions generally upholding confidentiality clauses and agreements. The governing law of the arrangement should also be clearly specified.

6.9.2 Outsourcing outside Singapore should be conducted in a manner so as not to hinder efforts to supervise or reconstruct the Singapore activities of the institution in a timely manner. Specifically, an institution should not outsource to jurisdictions where unfettered access to information by MAS or agents appointed by MAS to act on its behalf, and the internal and external auditors of the institution, may be impeded by legal or administrative restrictions. MAS may communicate directly with the home or host regulator of the institution or the service provider, as the case may be, to seek confirmation relating to these matters.

6.9.3 An institution should notify MAS if any overseas authority were to seek access to its customer information or where there are legal and administrative impediments to MAS accessing information of the Singapore office or information on a service provider. The institution may be required to terminate or make alternative outsourcing arrangements if confidentiality of its customer information or the ability of MAS to carry out its supervisory functions cannot be assured.

6.10 Outsourcing Within a Group

6.10.1 These guidelines are generally applicable to outsourcing to parties within an institution's group, including its HO or parent institution, another branch or related company. Similar to outsourcing to an unrelated party, the risk management practices expected to be adopted by a local office in a material outsourcing to a related party include establishing the details on the nature and scope of services provided, policies and

procedures relating to ownership and access, resolution of differences, sub-contracting, confidentiality and security, separation of property, business continuity management, monitoring of the performance and circumstances of the service provider and annual reviews to gauge compliance with agreed service levels, as described in paragraphs 6.1 to 6.9. There should be documentation in a service level agreement or an equivalent document, or policies and procedures, to govern the relationships, functions, obligations and responsibilities of the relevant parties within the group.

6.10.2 With regard to due diligence, an institution outsourcing to its HO or parent institution need not undertake a due diligence on the financial strength of these offices. Nevertheless, the other elements of the due diligence process outlined in paragraph 6.3 should be addressed. The local office may accept the due diligence performed by an affiliate if it were undertaken in the last 12 months.

6.11 Outsourcing of Internal Audit to External Auditors

6.11.1 Where the outsourced service is the internal audit function of an institution, there are additional issues that an institution should deliberate upon. One of these is the lack of independence or the appearance of impaired independence, when a service provider is handling multiple engagements for an institution, such as internal and external audits, and consulting work. There is doubt that the service provider, in its internal audit role, would criticise itself for the quality of the external audit or consultancy services provided to the institution. In addition, as operations of an institution are typically complex and involve large transaction volumes and amounts, it should ensure service providers have the proper expertise to adequately complete the engagement. An institution should address these and other relevant issues before the decision to outsource the internal audit function is taken.

6.11.2 Before outsourcing to external auditors, an institution should satisfy itself that the external auditor would be in compliance with the relevant auditor independence standards of the Singapore accounting profession.

Annex

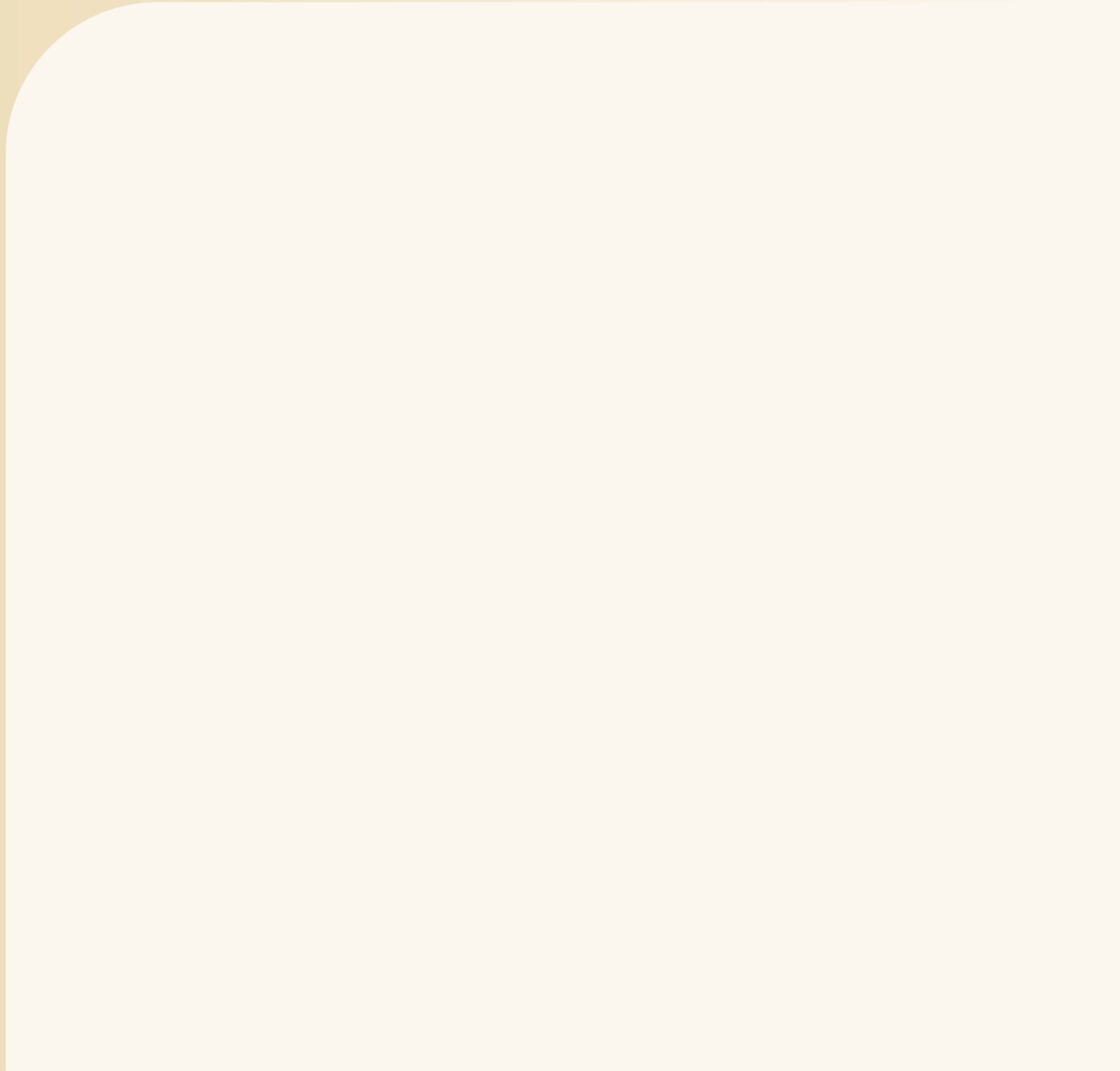
The following are examples of some services that, when performed by a third party, would be regarded as outsourcing for the purposes of the guidelines:-

- Application processing (e.g. loan origination, credit cards);
- Back office management (e.g. electronic funds transfer, payroll processing, custody operations, quality control, purchasing, maintaining the register of participants of a collective investment scheme (CIS) and sending of accounts and reports to CIS participants);
- Claims administration (e.g. loan negotiations, loan processing, collateral management, collection of bad loans);
- Document processing (e.g. cheques, credit card and bill payments, bank statements, other corporate payments);
- Information system management and maintenance (e.g. data entry and processing, data centres, facilities management, end-user support, local area networks, help desks);
- Investment management (portfolio management, cash management);
- Manpower management (e.g. benefits and compensation administration, staff appointment, training and development);
- Marketing and research (e.g. product development, data warehousing and mining, advertising, media relations, call centres, telemarketing);
- Professional services related to the business activities of the institution (e.g. accounting, internal audit, actuarial); and
- Real estate administration (e.g. building maintenance, lease negotiation, property evaluation, rent collection).

2 The following arrangements would generally not be considered outsourcing:

- Clearing and settlement arrangements between clearing and settlement institutions/houses and their members, and similar arrangements between members and non-members;
- Correspondent banking services;
- Credit background, background investigation and information services;
- Discreet advisory services (e.g. legal opinions, certain investment advisory services that do not result directly in investment decisions, independent appraisals, trustees in bankruptcy);

- Employment of contract or temporary personnel;
- Independent consulting;
- Market information services (e.g. Bloomberg, Moody's, Standard & Poors);
- Printing services;
- Purchase of goods, commercially available software and other commodities;
- Sale of insurance policies by agents or brokers;
- Services that the institution is not legally able to provide;
- Statutory audit and independent audit assessments; and
- Telephone, utilities, mail, courier services.



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