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### **CEBS Consultation - Outsourcing**

Regarding the consultation paper issued by the Committee of European Banking Supervisors we would like to inform you of the following considerations:

- The classification of activities as
  - (a) strategic or core activities which cannot be outsourced;
  - (b) non-strategic but material activities, which should be pre-notified to the supervisory authority; and
  - (c) non-strategic and non-material activities, which do not have to be pre-notified is, in principle, considered to be favourable.

It should not be overlooked that the definition of outsourcing versus purchasing should be made the subject of a principal analysis, in particular with regard to consulting services and customised solutions such as, e.g., EDP applications (see definition of purchasing).

- As stated in the accompanying text, in addition, a sub-classification and more detailed definition of the term "materiality" is desirable.
- Another central issue in connection with outsourcing will also be the extent to which co-operation and co-ordination of national supervisory authorities is warranted in case of cross-border outsourcing processes. If, for example, the national supervisory authority distinguishes between important and less important activities (which will also have regulatory consequences), different construction and interpretation may make cross-border solutions more difficult or even prevent them. Supervision of institutions which handle outsourcing activities but are domiciled in a different Member State may also be more difficult or prevented.

Thus, also a most detailed definition of strategic, material and non-strategic, non-material activities is necessary as well as a large coherence in the supervisory authority's interpretation. We must be aware of the fact that this will further accelerate the discussion on a transnational organisation of supervisory authorities (e.g., lead supervision).

As regards outsourcing policy and the contents of an outsourcing contract the differences between intra-group outsourcing and external outsourcing should be increasingly considered. Due to the parallels between contractual instruction relationship and corporate control the subject "contingency plan" and exit strategy in intra-group outsourcing is different from that in external outsourcing. Likewise the components of the contract should not only be proportionate to the risks and volume or complexity of the outsourced activity but it should also be considered whether, due to the parallels mentioned above, the outsourcing is an intra-group or an external one.

Currently, the issue of outsourcing is not only discussed with respect to credit institutions (and groups of credit institutions) in CEBS but also in CEPR. Here a coherence in principles should be created as well if we want to prevent that full-service banks get entangled in different statutory provisions.

- At the beginning of the paper it is pointed out that it is based on "current practices", i.e. all outsourcing systems common in the EU. However, a system based on the decentralised structure cannot be found in the paper. From the point of view of decentralised sectors it would therefore be necessary for the Austrian supervisors to introduce such systems in the relevant bodies. Proven and established decentralised banking systems should be allowed also in future. This concerns both co-operation among the different levels and co-operation at the same level.

In the case of decentralised sectors services in the group, such as, for example, the task of liquidity equalisation, are carried out by the top institution. However, this constitutes no outsourcing of an activity from a bank to another company but a prerequisite necessary for functioning within the group.

The paper distinguishes only between outsourcing to externals and intra-group outsourcing, with "intra-group" obviously meaning structures which are eventually subject to consolidation. The outsourcing system of decentralised sectors is not covered at all. The nature of the decentralised outsourcing system is that certain services of individual banks are covered by central sectoral companies jointly (e.g., payment transactions, securities, computing centres, etc.), which, according to the definition of the paper, can be called outsourcing. This does not, however, mean risk management tasks, with the exception of data pooling.

Now the consultation paper in our hands raises concerns that quite a lot of administrative work will be required in case of such structures (extensive contracts among all involved, approval by the supervisors, a "policy including contingency plans and exit strategies" for each credit institution, supervision of outsourced tasks, etc.).

To enter into SLAs with every single institution of a decentralised group that is organised by several levels would be uneconomical. For the major part of the services rendered for the associated institutions it must be possible to agree on SLAs through a central body authorised to do so. Only in this way can framework conditions for an efficient and economic operation be secured.

## **II. Core activities**

Risk management is not clearly defined by CP02. In our opinion an analogous definition by CEBS for the EU draft of a relevant directive would make sense.

Based on the principle that only non-core activities may be outsourced, outsourcing would be possible with respect to data pooling and development of rating models, but not the qualitative rating of a customer as such.

The position in favour thereof is also supported by the demand that responsibility for the outsourced activity must remain with the outsourcing institution.

- The classification into three categories is, in principle, considered reasonable; however, the distinguishing features of the definitions are still not clear enough to be used in practice and should be supplemented by examples and/or made more precise.
- As for the "weakest" category, non-strategic and non-material activities, it is stated that there will be no restrictions, but also here a number of rules are set up, which we consider to be too much in this area. Here the general rules on a bank's duty to exercise reasonable care should suffice.
- On the last but four page the paper mentions that an internal unit or individual should be specified that is responsible for supervising and managing each outsourcing measure.  
From this sentence we understand that one individual and/or department per outsourcing should be mainly responsible. This seems to be reasonable.  
However, if this sentence means that a new organisational unit should be set up for outsourcing, we object thereto because it cannot make sense to establish a separate unit and unnecessarily tie resources there, where it would be better for individuals from the area concerned to be responsible for outsourcing measures.
- p. 2 "The paper's primary focus is on financial institutions' own risk management in the area of outsourcing .."  
First of all, risk management should be defined. We propose the definition of EU-CP3 of 1 July 2003.
- p. 5 "... group-wide risk management refers to non-core functions ..."  
Since before risk management is defined as a core management function that cannot be outsourced, the question of the limit between core and non-core functions within risk management arises with respect to groups of banks. For example, outsourcing in the form of data pooling and developing of rating models is to be regarded as non-core; qualitative rating of a customer as such, however, is to be considered a core activity.
- p. 5 "... risk management function on a solo basis .."  
Here not only the solo level but also the subconsolidated level should be considered.
- p. 5 "In the case of outsourcing of non-core functions, domestic supervisory authorities, i.e. the host country, should also be involved in the decision to allow outsourcing, when needed."  
First, it is not clear why the authority should be involved in the decision on outsourcing of a non-core function and furthermore it is not clear what the passage "when needed" is supposed to mean.
- p. 6 "Outsourcing institutions should be aware that the supervisory authority may distinguish between important and less important activities, and may impose certain

conditions on institutions that outsource important activities."

At present, the paper lacks any examples of what "important" means. For the purpose of legal clarity and also of a level playing field, at first a most comprehensive catalogue should be prepared. For the remaining area at least a common method should be developed: under "Further work" (p. 2) a "concept of a materiality test" that is yet to be prepared is mentioned ("some jurisdictions operate a scoring system to assess materiality").

- p. 8 and 9 Contingency plans and exit strategies  
In the case of intra-group outsourcing the fact should be considered that this problem is of a different dimension than in the case of external outsourcing.
- p. 10 "When drafting the contract the outsourcing institution should bear in mind that the level of ... should be proportionate to the risks involved and the size and complexity of the outsourced activity"  
Here, too, account should be taken of whether the outsourcing is an intra-group or external one.
- p. 10 ".. to give effective rights of access to information to the supervisory authority. This may require obtaining consents from affected parties such as the parent company and relevant home supervisory authorities"  
If this means that in the case of intra-group outsourcing an approval from the parent bank and its supervisor might be required, this should be explained in more detail and reasons should be given.

Yours sincerely,

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