

## Mapping of outsourcing requirements

Following comments received during the first round of consultation, CEBS and the Committee of European Securities Regulators (CESR) have worked closely together to ensure that the proposed standards are consistent with the Markets in Financial Instruments Directive (MiFID) and its application to credit institutions. CEBS has strived to align the proposed standards to the highest degree possible with regulation under MiFID.

The table below contains a mapping of the present version of CEBS Standards, CESR's Technical Advice on MiFID and the final version of the European Commission MiFID Level 2 measures.

| <p><b>CEBS Guidelines on Outsourcing<br/>(December 2006)</b></p>   | <p><b>CESR's Technical Advice on<br/>Possible Implementing Measures of<br/>the Directive 2004/39/EC on Markets in Financial<br/>Instruments (MIFID)<br/>1<sup>st</sup> Set of Mandates – January 2005</b></p> <p><b>Section I Definitions<br/>Section II Intermediaries</b></p> <p><b>Note: the text of CESR's TA as printed in this column<br/>does not follow its own numbering, but has been cut<br/>in as much pieces as to allow proper comparison<br/>with the CEBS paper.</b></p>  | <p><b>Commission Directive 2006/73/EC<br/>of 10 August 2006<br/>(published on 2 September 2006)</b></p> <p><b>implementing Directive 2004/39/EC of the<br/>European Parliament and of the Council as regards<br/>organisational requirements and operating<br/>conditions for investment firms, and defined terms<br/>for the purposes of that Directive</b></p> |
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| <p>CEBS presents its Guidelines on Outsourcing. The proposed guidelines are based on current practices and also take into account international, such as the Joint Forum, and European initiatives in the field of outsourcing. Following comments received during the first round of consultation, CEBS and the Committee of European Securities Regulators (CESR) have ensured that the proposed guidelines are consistent with the Markets in Financial Instruments Directive (MiFID) and its application to credit institutions.</p> <p><b>Introduction</b></p> <p>There is currently no harmonisation at the EU level in the area of outsourcing undertaken by credit institutions and, accordingly, different supervisory approaches have developed across the EU to address the potential risks arising from this practice. A number of European countries have, for some years, had in place formal outsourcing regimes. Given the increasing use of outsourcing by institutions, including on a cross-border basis, and its</p> | <p><b>Extract from the Mandate of the Commission to CESR (Level 2)</b></p> <p>DG Internal Market requests CESR to provide technical advice on possible implementing measures by 31 January 2005 on following issues:</p> <p>(1) Determine what is meant by operational functions; establish the criteria for determining which functions are critical for the provision of continuous and satisfactory service to clients and the performance of investment activities on a continuous and satisfactory basis.</p> <p>(2) Establish the conditions to which the firm is subject and the arrangements to put in place, when outsourcing its operational functions.</p> <p>(3) Specify what is to be considered as outsourcing for the purposes of this rule.</p> |  |

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| <p>implications for effective prudential supervision, CEBS has deemed it appropriate to develop these Guidelines in order to promote greater consistency of approach where possible within the national legal frameworks. The Guidelines are based on a range of current practices and the common elements of policy that have been elaborated to date in various Member States but also take into account various recent international and European initiatives in the field of outsourcing.</p> <p>There is an obvious overlap between the proposed guidelines, on the one hand, and relevant MiFID rules, and the ensuing Level 2 measures that will apply to all authorized entities offering investment services under the MiFID, on the other hand. CEBS and CESR have duly consulted to ensure that the proposed guidelines:</p> <ul style="list-style-type: none"> <li>• are in full compliance with the MiFID Level 2 provisions and that their application to credit institutions subject to MiFID is fully consistent; and</li> <li>• are consistently applied to all credit institutions, thus contributing towards establishing a level playing field for them.</li> </ul> <p>These Guidelines are designed to promote an appropriate level of convergence in supervisory practices throughout the EU. At the same time, the Guidelines are principles-based and provide national supervisors with an adequate degree of flexibility to take into account domestic rules and specific features of their local markets and to accommodate developments in market practices.</p> <p>The concept of proportionality, as laid down in the provisions of the Directive 2006/48/EC applies also to outsourcing and its policy which will be expected to be related to the size of the institutions as well as to the sophistication and diversification of the outsourcing activities. Supervisory authorities will adapt their approach to outsourcing to ensure it is proportionate to the nature, scale and complexity of the outsourced activities of an institution.</p> |  |  |
| <p>Scope of application: authorised entity</p>   | <p>Scope of application: investment firms, regulated markets and credit institutions which provide investment services and/or activities.</p> <p><b>Article 1 MIFID: Scope</b></p> <p>1. This Directive shall apply to investment firms and regulated markets.</p> <p>2. The following provisions shall also apply to credit institutions authorised under Directive 2000/12/EC, when providing one or more investment services and/or</p> | <p><b>Article 1(2)</b></p> <p>Chapter II and Sections 1 to 4, Article 45 and Sections 6 and 8 of Chapter III, to the extent they relate to those provisions, Chapter I and Section 9 of Chapter III and Chapter IV of this Directive shall apply to shall apply to management companies in accordance with Article 5(4) of Council Directive 85/611/EEC.</p> |

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|   | <p>performing investment activities:</p> <ul style="list-style-type: none"> <li>- Articles 2(2), 11, 13 and 14,</li> <li>- Chapter II of Title II excluding Article 23(2) second subparagraph,</li> <li>- Chapter III of Title II excluding Articles 31(2) to 31(4) and 32(2) to 32(6), 32(8) and 32(9),</li> <li>- Articles 48 to 53, 57, 61 and 62, and</li> <li>- Article 71(1).</li> </ul> |   |
| <p style="text-align: center;"><b>Chapter 1: Definitions</b></p> <p style="text-align: center;"><b>Guideline 1</b></p> <p>For the purposes of these guidelines, the following is meant by:</p> <p>a. outsourcing: an authorised entity's use of a third party (the "outsourcing service provider") to perform activities that would normally be undertaken by the authorised entity, now or in the future. The supplier may itself be an authorised or unauthorised entity;</p> | <p><b>BOX 1 – Definitions</b></p> <p>6 "outsourcing" means all forms of arrangements which involve an investment firm relying on a third party service provider for the performance of a process, a service or an activity that would otherwise be undertaken by the investment firm itself</p>  | <p><b>Article 2(6)</b></p> <p>"outsourcing" means an arrangement of any form between an investment firm and a service provider by which that service provider performs a process, a service or an activity which would otherwise be undertaken by the investment firm itself;</p> <p><b>Recital 18</b></p> <p>Competent authorities should not make the authorisation to provide investment services or activities subject to a general prohibition on the outsourcing of one or more critical or important functions or investment services or activities. Investment firms should be allowed to outsource such activities if the outsourcing arrangements established by the firm comply with certain conditions.</p> |
| <p>b. purchasing: <i>inter alia</i>, the supply (i) of services, goods or facilities without information about, or belonging to, the purchasing institution coming within the control of the supplier; or (ii) of standardized products, such as market information or office inventory (authorised entities should ensure that what they are buying is fit for purpose). The supply of (i) or (ii) is not outsourcing;</p>   |  |   |
| <p>c. outsourcing service provider: the supplier of goods, services or facilities, which may or may not be an authorised entity, and which may be an affiliated entity within a corporate group or an entity that is external to the group;</p>   |  |   |
| <p>d. outsourcing institution: the authorised entity which is the buyer of such goods, services or facilities;</p>  |  |   |
| <p>e. authorised entity: a licensed credit institution;</p>   |  |   |
| <p>f. material activities: (i) activities of such importance that any weakness or failure in the</p>  | <p><b>Box 4</b></p>  | <p><b>Article 13(1) and (2) (Meaning of critical and</b></p>  |

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| <p>provision of these activities could have a significant effect on the authorised entity's ability to meet its regulatory responsibilities and/or to continue in business; (ii) any other activities requiring a licence from the supervisory authority; (iii) any activities having a significant impact on its risk management; and (iv) the management of risks related to these activities.</p> | <p><b>Obligations to avoid undue additional operational risk in case of outsourcing</b></p> <p><b>Application to material outsourcing only</b></p> <p>1. This advice only applies to outsourcing arrangements pertaining to operational functions where a weakness or failure in the performance of the outsourced functions would cast serious doubt upon the investment firm's continuing compliance with the conditions and obligations of its authorization and/or upon its financial performance, financial position or continuity of operations.</p> <p>2. Subject to paragraphs 1 and 4, outsourcing of the following functions is included in the scope of application of this advice: accounting, back office, information technology and information system management and maintenance, marketing and research, services related to the internal audit, compliance and risk control functions.</p> <p><b>Application to intra-group outsourcing</b></p> <p>3. This advice also applies to intra-group outsourcing where the arrangements meet the conditions set out in paragraph 1 subject to paragraph 4.</p> <p><b>Arrangements not included</b></p> <p>4. Notwithstanding the paragraphs 1 to 3, this advice does not apply to outsourcing of the following:</p> <ul style="list-style-type: none"> <li>(a) discrete advisory services, such as the provision of legal advice, procurement of specialized training, billing and physical security;</li> <li>(b) supply arrangements and functions, such as the provision of electricity, water, catering, and cleaning;</li> <li>(c) investment services and activities;</li> <li>(d) the purchase of standardised services such as market information services and provision of prices; and</li> <li>(e) the use of depositories under arrangements falling within Articles 13(7) and (8) of the Directive.</li> </ul> | <p><b>important operational functions)</b></p> <p>1. For the purposes of the first subparagraph of Article 13(5) of Directive 2004/39/EC, an operational function shall be regarded as critical or important if a defect or failure in its performance would materially impair the continuing compliance of an investment firm with the conditions and obligations of its authorisation or its other obligations under Directive 2004/39/EC, or its financial performance, or the soundness or the continuity of its investment services and activities.</p> <p>2. Without prejudice to the status of any other function, the following functions shall not be considered as critical or important for the purposes of paragraph 1:</p> <ul style="list-style-type: none"> <li>(a) the provision to the firm of advisory services, and other services which do not form part of the investment business of the firm, including the provision of legal advice to the firm, the training of personnel of the firm, billing services and the security of the firm's premises and personnel;</li> <li>(b) the purchase of standardised services, including market information services and the provision of price feeds.</li> </ul> |
| <p>g. senior management: persons who effectively direct the business of the authorised entity;</p>   |   |   |
| <p>h. "chain" outsourcing: outsourcing where the outsourcing service provider subcontracts elements of the service to other providers.</p>   |   |   |

| <p align="center"><b>Chapter 2:<br/>Guidelines on outsourcing addressed to<br/>authorised entities</b></p>  |   |   |
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| <p align="center"><b>Guideline 2</b></p> <p><b>The ultimate responsibility for the proper management of the risks associated with outsourcing or the outsourced activities lies with an outsourcing institution's senior management.</b></p> <ol style="list-style-type: none"> <li>1. All outsourcing regimes should ensure that the outsourcing of functions to an outsourcing service provider does not impair the supervision of the outsourcing institution.</li> <li>2. Responsibility for outsourced functions must always be retained by the outsourcing institution. The outsourcing of functions does not relieve an outsourcing institution of its regulatory responsibilities for its authorized activities or the function concerned.</li> <li>3. Outsourcing institutions should be required to retain adequate core competence at a senior operational level in house to enable them to have the capability to resume direct control over an outsourced activity, in extremis.</li> <li>4. Outsourcing shall not affect managers' full and unrestricted responsibilities under applicable legislation (e.g. under banking law).</li> </ol> | <p><b>General obligation of due skill, care and diligence</b></p> <p>7. An investment firm must exercise due skill, care and diligence in planning, entering into, managing and exiting from any outsourcing. To this end it must identify, assess, monitor and manage the risks inherent in outsourcing and take reasonable steps to avoid or mitigate the impact that outsourcing might have on its exposure to operational risk.</p> <p><b>Specific obligations</b></p> <p>8. In complying with its obligations under paragraph 7, the measures to be taken by the investment firm include the following:</p> <ol style="list-style-type: none"> <li>(a) the investment firm must ensure that senior management approves and periodically reviews the investment firm's policy for outsourcing operational functions; this includes the assessment of feasibility, of risk and of the impact on business and costs, as well as the definition of criteria for selecting the service providers;</li> <li>(b) (...);</li> <li>(c) the investment firm must retain the required expertise to effectively supervise the outsourced functions and manage the risks associated with the outsourcing; senior management should take appropriate action if cause for concern arises;</li> </ol> <p>(...)</p> | <p><b>Article 14(1) and (2) (Conditions for outsourcing critical or important operational functions or investment services or activities)</b></p> <p>1. Member States shall ensure that, when investment firms outsource critical or important operational functions or any investment services or activities, the firms remain fully responsible for discharging all of their obligations under Directive 2004/39/EC and comply, in particular, with the following conditions:</p> <ol style="list-style-type: none"> <li>(a) the outsourcing must not result in the delegation by senior management of its responsibility;</li> <li>(b) the relationship and obligations of the investment firm towards its clients under the terms of Directive 2004/39/EC must not be altered;</li> <li>(c) the conditions with which the investment firm must comply in order to be authorised in accordance with Article 5 of Directive 2004/39/EC, and to remain so, must not be undermined;</li> <li>(d) none of the other conditions subject to which the firm's authorisation was granted must be removed or modified.</li> </ol> <p>2. Member States shall require investment firms to exercise due skill, care and diligence when entering into, managing or terminating any arrangement for the outsourcing to a service provider of critical or important operational functions or of any investment services or activities.</p> <p>Investment firms shall in particular take the necessary steps to ensure that the following conditions are satisfied:</p> <ol style="list-style-type: none"> <li>(a) the service provider must have the ability, capacity, and any authorisation required by law to perform the outsourced functions, services or activities reliably and professionally;</li> <li>(b) the service provider must carry out the outsourced services effectively, and to this end the firm must establish methods for assessing the standard of performance of the service provider;</li> <li>(c) the service provider must properly supervise the carrying out of the outsourced functions, and adequately manage the risks associated with the outsourcing;</li> <li>(d) appropriate action must be taken if it appears that the service provider may not be carrying out the</li> </ol> |

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|  |   | <p>functions effectively and in compliance with applicable laws and regulatory requirements;</p> <p>(e) the investment firm must retain the necessary expertise to supervise the outsourced functions effectively and manage the risks associated with the outsourcing and must supervise those functions and manage those risks;</p> <p>(f) the service provider must disclose to the investment firm any development that may have an impact on its ability to carry out the outsourced functions effectively and in compliance with applicable laws and regulatory requirements;</p> <p>(g) the investment firm must be able to terminate the arrangement for outsourcing where necessary without detriment to the continuity and quality of its provision of services to clients;</p> <p>(h) the service provider must cooperate with the competent authorities of the investment firm in connection with the outsourced activities;</p> <p>(i) the investment firm, its auditors and the relevant competent authorities must have effective access to data related to the outsourced activities, as well as to the business premises of the service provider; and the competent authorities must be able to exercise those rights of access;</p> <p>(j) the service provider must protect any confidential information relating to the investment firm and its clients;</p> <p>(k) the investment firm and the service provider must establish, implement and maintain a contingency plan for disaster recovery and periodic testing of backup facilities, where that is necessary having regard to the function, service or activity that has been outsourced.</p> |
| <p align="center"><b>Guideline 3</b></p> <p><b>Outsourcing arrangements can never result in the delegation of senior management’s responsibility.</b></p> <p>1. The outsourcing of core management functions is considered generally to be incompatible with the senior management’s obligation to run the enterprise under their own responsibility. Core management functions include, inter alia, setting the risk strategy, the risk policy, and, accordingly, the risk-bearing capacity of the institution. Hence, management functions such as the setting of strategies and policies in respect of the authorised entity’s risk</p> | <p><b>BOX 4</b></p> <p><b>Effect of outsourcing on the position of the investment firm</b></p> <p>5. Outsourcing does not release the investment firm from its regulatory obligations and cannot result in the delegation of senior management’s responsibility. Outsourcing does not alter the relationship and obligations of the investment firm under the terms of the Directive towards its clients. Outsourcing must not be undertaken in such a way that it undermines the assumptions and conditions on which the</p> | <p><b>Article 14(1) (Conditions for outsourcing critical or important operational functions or investment services or activities)</b></p> <p>Member States shall ensure that, when investment firms outsource critical or important operational functions or any <del>other</del> investment services or activities, the firms remain fully responsible for discharging all of their obligations under Directive 2004/39/EC and comply, in particular, with the following conditions:</p> <p>(a) the outsourcing must not result in the delegation by senior management of its responsibility;</p> <p>(b) the relationship and obligations of the investment</p>   |

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| <p>profile and control, the oversight of the operation of the entity's processes, and the final responsibility towards customers and supervisors should not be outsourced.</p>   | <p>investment firm's authorization is based.</p>  | <p>firm towards its clients under the terms of Directive 2004/39/EC must not be altered;</p> <p>(c) the conditions with which the investment firm must comply in order to be authorised in accordance with Article 5 of Directive 2004/39/EC, and to remain so, must not be undermined;</p> <p>(d) none of the other conditions subject to which the firm's authorisation was granted must be removed or modified.</p> <p><b>Recital 19</b></p> <p>For the purposes of the provisions of this Directive setting out conditions for outsourcing critical or important operational functions or investment services or activities, an outsourcing that would involve the delegation of functions to the extent that the firm becomes a letter box entity should be considered to undermine the conditions with which the investment firm must comply in order to be and remain authorised in accordance with Article 5 of Directive 2004/39/EC.</p>   |
| <p style="text-align: center;"><b>Guideline 4</b></p> <p><b>4.1 An authorised entity may not outsource services and activities concerning the acceptance of deposits or to lending requiring a licence from the supervisory authority according to the applicable national banking law unless the outsourcing service provider either (i) has an authorisation that is equivalent to the authorisation of the outsourcing institution; or (ii) otherwise allowed to carry out those activities in accordance with the relevant national legal framework.</b></p> | <p><b>BOX 4 – Extract</b></p> <p>5. (...) Outsourcing must not be undertaken in such a way that it undermines the assumptions and conditions on which the investment firm's authorisation is based.</p> <p><b>BOX 1 – Extract "Outsourcing pertaining to investment services and activities"</b></p> <p>15. Where outsourcing arrangements or intended outsourcing arrangements pertain to investment services and/or activities:</p> <p>(a) paragraphs 3 and 5 to 8 of the advice on the first paragraph of Article 13(5) of the Directive shall apply to such arrangements; and</p> <p>(b) where the outsourcing involves the <b>delegation of the portfolio management function</b> to a service provider located in a third country</p> <p>(i) that service provider must be authorised in its home country to provide that service;</p> <p>and</p> <p>(ii) there must be an appropriate formal arrangement between regulators that enables them to exchange material information concerning both cross-border outsourcings and the service provider.</p> | <p><b>Article 15 (Service providers located in third countries)</b></p> <p>1. In addition to the requirements set out in Article 14, Member States shall require that, where an investment firm outsources the investment service of portfolio management provided to retail clients to a service provider located in a third country, that investment firm ensures that the following conditions are satisfied:</p> <p>(a) the service provider must be authorised or registered in its home country to provide that service and must be subject to prudential supervision;</p> <p>(b) there must be an appropriate cooperation agreement between the competent authority of the investment firm and the supervisory authority of the service provider.</p> <p>2. Where one or both of those conditions mentioned in paragraph 1 are not satisfied, an investment firm may outsource investment services to a service provider located in a third country only if the firm gives prior notification to its competent authority about the outsourcing arrangement and the competent authority does not object to that arrangement within a reasonable time following receipt of that notification.</p> <p>3. Without prejudice to paragraph 2, Member States shall publish or require competent authorities to publish a statement of policy in relation to outsourcing covered by paragraph 2. That statements shall set out examples of cases where the competent authority would not, or would</p> |

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|  |  | <p>be likely not to, object to an outsourcing under paragraph 2 where one or both of the conditions in points (a) and (b) of paragraph 1 are not met. It shall include a clear explanation as to why the competent authority considers that in such cases outsourcing would not impair the ability of investment firms to fulfil their obligations under Article 14.</p> <p>4. Nothing in this article limits the obligations on investment firms to comply with the requirements in Article 14.</p> <p>5. Competent authorities shall publish a list of the supervisory authorities in third countries with which they have cooperation agreements that are appropriate for the purposes of point (b) of paragraph 1.</p> |
| <p><b>4.2 Any area of activity of an outsourcing institution other than those identified in Guidelines 2 and 3 may be outsourced provided that such outsourcing does not impair:</b></p> <ul style="list-style-type: none"> <li><b>a. the orderliness of the conduct of the outsourcing institution's business or of the financial services provided;</b></li> <li><b>b. the senior management's ability to manage and monitor the authorised entity's business and its authorised activities;</b></li> <li><b>c. the ability of other internal governance bodies, such as the board of directors or the audit committee, to fulfil their oversight tasks in relation to the senior management; and</b></li> <li><b>d. the supervision of the outsourced institution.</b></li> </ul> |  | <p><b>Recital 18</b></p> <p>Competent authorities should not make the authorisation to provide investment services or activities subject to a general prohibition on the outsourcing of one or more critical or important functions or investment services or activities. Investment firms should be allowed to outsource such activities if the outsourcing arrangements established by the firm comply with certain conditions.</p>  |
| <p><b>4.3 An outsourcing institution should take particular care when outsourcing material activities. The outsourcing institution should adequately inform its supervisory authority about this type of outsourcing.</b></p>  | <p><b>BOX 4</b></p> <p><b>Notification of material outsourcing to competent authority</b></p> <p>6. Subject to paragraphs 1 and 4, an investment firm must provide the competent authority with prior notification of its intention to outsource and make available on request of the competent authority all relevant information, enabling it to effectively exercise its supervision in respect of the provisions referred to in this advice.</p> | <p><b>Article 14(5)</b></p> <p>Member States shall require investment firms to make available on request to the competent authority all information necessary to enable the authority to supervise the compliance of the performance of the outsourced activities with the requirements of this Directive.</p> <p><b>Recital 20</b></p> <p>The outsourcing of investment services or activities or critical and important functions is capable of constituting a material change of the conditions for the authorisation of the investment firm, as referred to in Article 16(2) of Directive 2004/39/EC. If such outsourcing arrangements are to be put in place after the investment firm has</p>                        |



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|   |  | <p>obtained an authorisation according to the provisions included in Chapter I of Title II of Directive 2004/39/EC, those arrangements should be notified to the competent authority where required by Article 16(2) of Directive 2004/39/EC.</p> <p><b>Recital 21</b></p> <p>Investment firms are required by this Directive to give the responsible competent authority prior notification of any arrangement for the outsourcing of the management of retail client portfolios that it proposes to enter into with a service provider located in a third country, where certain specified conditions are not met. However, competent authorities are not expected to authorise or otherwise approve any such arrangement or its terms. The purpose of the notification, rather, is to ensure that the competent authority has the opportunity to intervene in appropriate cases. It is the responsibility of the investment firm to negotiate the terms of any outsourcing arrangement, and to ensure that those terms are consistent with the obligations of the firm under this Directive and Directive 2004/39/EC, without the formal intervention of the competent authority.</p> |
| <p>1. These requirements do not affect the principle of managers' sole responsibility (Guideline 2) for all authorised activities. The managers of the outsourcing institution shall be fully responsible to the supervisory authority for any outsourced activity. The managers should therefore take suitable measures to ensure that the outsourced activities continue to meet the performance and quality guidelines that would apply if their own institution were to perform the relevant activities in-house.</p> <p>2. An outsourcing institution should adequately inform its supervisory authority on any material activity to be outsourced. Such information should be made available in a timely manner in order for the supervisor to evaluate the proposal or to allow him to consider whether the proposal raises prudential concerns and to take appropriate action if required. Outsourcing institutions should be aware that for the outsourcing of material activities the supervisory authority may impose specific conditions. In doing so, the supervisory authority will consider factors such as the size of the institution, the nature of the outsourced activity, the characteristics and market position of the service provider, the duration of the contract and the potential of the outsourcing to generate conflicts of interest (e.g. the supervisory</p> | <p><b>BOX 4 - Extracts</b></p> <p><b>Effect of outsourcing on the position of the investment firm</b></p> <p>5. Outsourcing does not release the investment firm from its regulatory obligations and cannot result in the delegation of senior management's responsibility. Outsourcing does not alter the relationship and obligations of the investment firm under the terms of the Directive towards its clients.</p> <p>Outsourcing must not be undertaken in such a way that it undermines the assumptions and conditions on which the investment firm's authorisation is based.</p> <p><b>General obligation of due skill, care and diligence</b></p> <p>7. An investment firm must exercise due skill, care and diligence in planning, entering into, managing and exiting from any outsourcing. To this end it must identify, assess, monitor and manage the risks inherent in outsourcing and take reasonable steps to avoid or mitigate the impact that outsourcing might have on its exposure to operational risk.</p> <p><b>Specific obligations</b></p> | <p><b>Article 14(1) and (2) (Conditions for outsourcing critical or important operational functions or investment services or activities)</b></p> <p>1. Member States shall ensure that, when investment firms outsource critical or important operational functions or any investment services or activities, the firms remain fully responsible for discharging all of their obligations under Directive 2004/39/EC and comply, in particular, with the following conditions:</p> <p>(a) the outsourcing must not result in the delegation by senior management of its responsibility;</p> <p>(...)</p> <p>2. Member States shall require investment firms to exercise due skill, <del>and</del> care and diligence when entering into, managing or terminating any arrangement for the outsourcing to a service provider of critical or important operational functions or of any investment services or activities. Investment firms shall in particular take the necessary steps to ensure that the following conditions are satisfied:</p> <p>(...)</p> <p>(c) the service provider must properly supervise the carrying out of the outsourced functions, and</p>                  |

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| <p>authority may wish to prohibit the outsourcing of the financial accounting and the preparation of the annual accounts to the outsourcing institution's external auditor, or to the office with which the external auditor is connected).</p> <p>3. An outsourcing institution should inform its supervisory authority of any material development affecting the service provider and its ability to fulfil its obligations to customers.</p> <p>4. Subject to the principles that apply to cross-border outsourcing expressed under Guideline 4.1(i), no special rules are needed in relation to the geographical location of an outsourcing service provider. However, due to possible data protection risks and risks to effective supervision by the supervisory authority, institutions should take special care when entering into and managing outsourcing agreements that are undertaken outside the EEA.</p> | <p>8. In complying with its obligations under paragraph 7, the measures to be taken by the investment firm include the following:</p> <p>(a) the investment firm must ensure that senior management approves and periodically reviews the investment firm's policy for outsourcing operational functions; this includes the assessment of feasibility, of risk and of the impact on business and costs, as well as the definition of criteria for selecting the service providers; (...)</p> <p>(c) the investment firm must retain the required expertise to effectively supervise the outsourced functions and manage the risks associated with the outsourcing; senior management should take appropriate action if cause for concern arises; (...)</p>  | <p>adequately manage the risks associated with the outsourcing;</p> <p>(d) appropriate action must be taken if it appears that the service provider may not be carrying out the functions effectively and in compliance with applicable laws and regulatory requirements;</p> <p>(e) the investment firm must retain the necessary expertise to supervise the outsourced functions effectively and manage the risks associated with the outsourcing and must supervise those functions and manage those risks;</p> |
| <p>5. Intra-group outsourcing and outsourcing according to Guideline 4.1(i) can be material. Outsourcing institutions should be aware that supervisory authorities may take specific circumstances into consideration, such as the extent to which the outsourcing institution controls the service provider or has the ability to influence its actions, and the extent to which the service provider is included in the consolidated supervision of the group, when assessing the risks associated with an intra-group outsourcing arrangement and the treatment to apply to such arrangements.</p>   | <p><b>BOX 4</b><br/> <b>Extract from § 3</b><br/> <b>Application to intra-group outsourcing</b></p> <p>This advice also applies to intra-group outsourcing where the arrangements meet the conditions set out in paragraph 1 subject to paragraph 4.</p> <p>However, the measures to be taken by the investment firm in accordance with paragraph 8 of this advice in respect of due diligence (indent b), monitoring of risk (indent c) or exit strategies (indents d(vii) and e), may take into account the group dimension, including factors such as the degree to which the investment firm controls the service provider or that it has the ability to influence its actions, or the fact that the service provider is included in the supervision on a consolidated basis of the investment firm's group, or is itself subject to authorisation or supervision.</p> <p>The investment firm must be able to demonstrate to the competent authority that the gearing of the measures implemented by the firm referred to under paragraph 8 is appropriate and proportionate to the factors taken into account.</p> | <p><b>Article 14(4)</b></p> <p>Member States shall provide that, where the investment firm and the service provider are members of the same group, the investment firm may, for the purposes of complying with this Article and Article 15, take into account the extent to which the firm controls the service provider or has the ability to influence its actions.</p>  |
| <p><b>Guideline 5</b></p> <p><b>There should be no restrictions on the outsourcing of non-material activities of an outsourcing institution.</b></p> <p>1. In such cases the outsourcing institution does not need to adequately inform its supervisory authority. Nevertheless, outsourcing institutions should</p>  |   | <p><b>Article 13(1) and (2) (Meaning of critical and important operational functions)</b></p> <p>1. For the purposes of the first subparagraph of Article 13(5) of Directive 2004/39/EC, an operational function shall be regarded as critical or important if a defect or failure in its performance would materially impair the continuing compliance of an investment firm with the</p>   |

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| <p>adequately manage the risks relating to such outsourcing arrangements at all times. In line with Guideline 2, the senior management of the outsourcing institution should be fully responsible for any outsourced activity.</p> <p>2. Areas which could be regarded as non-material are those not falling within the definition of "material activities" according to Guideline 1(f), and may include:</p> <p>a. areas which do not potentially constitute relevant risks and which, if outsourced, would not compromise the provisions set forth in Guideline 4.2 above; and</p> <p>b. purely advisory services used by the institution. For example, this applies to legal and tax consulting, even where this is not limited to individual aspects or projects.</p>   |   | <p>conditions and obligations of its authorisation or its other obligations under Directive 2004/39/EC, or its financial performance, or the soundness or the continuity of its investment services and activities.</p> <p>2. Without prejudice to the status of any other function, the following functions shall not be considered as critical or important for the purposes of paragraph 1:</p> <p>(a) the provision to the firm of advisory services, and other services which do not form part of the investment business of the firm, including the provision of legal advice to the firm, the training of personnel of the firm, billing services and the security of the firm's premises and personnel;</p> <p>(b) the purchase of standardised services, including market information services and the provision of price feeds.</p>  |
| <p style="text-align: center;"><b>Guideline 6</b></p> <p><b>6.1 The outsourcing institution should have a policy on its approach to outsourcing, including contingency plans and exit strategies.</b></p> <p><b>6.2 An outsourcing institution should conduct its business in a controlled and sound manner at all times.</b></p> <p>1. The outsourcing institution should have a general policy that covers all aspects of outsourcing, including non-material outsourcing, whether the outsourcing takes place within a corporate group or not.</p> <p>2. When drawing up the policy the outsourcing institutions should recognise that no form of outsourcing is risk free. The policy should recognise that the management of non-material and intra-group outsourcing should be proportionate to the risks presented by these arrangements.</p> <p>3. The policy should explicitly consider the potential effects of outsourcing on certain significant functions (e.g. the internal audit function and the compliance function) when conducting the risk analysis prior to outsourcing.</p> <p>4. The policy should ensure that the outsourcing service provider's financial performance and essential changes in the service provider's organisation structure and ownership structure are appropriately monitored and assessed by the outsourcing institution's management so that any necessary corrective measures can be taken promptly.</p> <p>5. The outsourcing institution should specify the internal</p> | <p><b>BOX 4 - Extracts</b></p> <p>7. An investment firm must exercise due skill, care and diligence in planning, entering into, managing and exiting from any outsourcing. To this end it must identify, assess, monitor and manage the risks inherent in outsourcing and take reasonable steps to avoid or mitigate the impact that outsourcing might have on its exposure to operational risk.</p> <p>8. In complying with its obligations under paragraph 7, the measures to be taken by the investment firm include the following:</p> <p>(a) the investment firm must ensure that senior management approves and periodically reviews the investment firm's policy for outsourcing operational functions; this includes the assessment of feasibility, of risk and of the impact on business and costs, as well as the definition of criteria for selecting the service providers;</p> <p>(b) the investment firm must ensure that the service provider has the ability and capacity to perform the outsourced functions reliably and professionally. To that end, the investment firm must evaluate the service provider and its services at the start and during the life cycle of the outsourcing. In performing this evaluation, the matters of which the investment firm should take particular account include where relevant, whether the service provider is regulated, to what extent and by whom, including whether the provision of the outsourced functions is subject to specific regulation or supervision, and the risk that the requested services are not available due to the number of other persons using the same</p> | <p><b>Article 14(2) (Conditions for outsourcing critical or important operational functions or investment services or activities)</b></p> <p>Member States shall require investment firms to exercise due skill and care and diligence when entering into, managing or terminating any arrangement for the outsourcing to a service provider of critical or important operational functions or of any investment services or activities. Investment firms shall in particular take the necessary steps to ensure that the following conditions are satisfied:</p> <p>(...)</p> <p>(f) the service provider must disclose to the investment firm any development that may have an impact on its ability to carry out the outsourced functions effectively and in compliance with applicable laws and regulatory requirements;</p> <p>(g) the investment firm must be able to terminate the arrangement for outsourcing where necessary without detriment to the continuity and quality of its provision of services to clients.</p> <p>(...)</p> <p>(k) the investment firm and the service provider must establish, implement and maintain a contingency plan for disaster recovery and periodic testing of backup facilities, where that is necessary having regard to the function, service or activity that has been outsourced .</p> |

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| <p>units or individuals that are responsible for monitoring and managing each outsourcing arrangement.</p> <p>6. The policy should consider the main phases that make up the life cycle of an institution's outsourcing arrangements:</p> <ul style="list-style-type: none"> <li>a. the decision to outsource or change an existing outsourcing arrangement (the decision making phase);</li> <li>b. due diligence checks on the outsourcing service provider;</li> <li>c. drafting a written outsourcing contract and service level agreement (the contract drafting phase);</li> <li>d. the implementation, monitoring, and management of an outsourcing arrangement (the contractual phase). This may include also the following-up of changes affecting the outsourcing service provider (e.g. major change in ownership, strategies, profitability of operations);</li> <li>e. dealing with the expected or unexpected termination of a contract and other service interruptions (the post-contractual phase). In particular, outsourcing institutions should plan and implement arrangements to maintain the continuity of their business in the event that the provision of services by an outsourcing service provider fails or deteriorates to an unacceptable degree, or the firm experiences other changes. This policy should include contingency planning and a clearly defined exit strategy.</li> </ul> | <p>service provider;</p> <ul style="list-style-type: none"> <li>(c) the investment firm must retain the required expertise to effectively supervise the outsourced functions and manage the risks associated with the outsourcing; senior management should take appropriate action if cause for concern arises;</li> <li>(d) the parties' respective responsibilities in relation to outsourcing must be clearly allocated in a written agreement; such agreement must also include, if applicable and where appropriate having regard to the function outsourced: <ul style="list-style-type: none"> <li>(i) the law applicable to the contract;</li> <li>(ii) the relevant code of conduct and the compliance function in charge of monitoring its application;</li> <li>(iii) the obligation to protect confidential information;</li> <li>(iv) the obligation for the service provider to disclose material developments that may have an impact on the outsourced functions;</li> <li>(v) the contingency procedures;</li> <li>(vi) where permitted by national law and by the contract, the rules for subcontracting for the service provider;</li> <li>(vii) the termination rights of both parties; and</li> <li>(viii) the methods for measuring, and procedures for reporting, the quantitative and qualitative performance by the service provider, in order to enable the investment firm to assess the adequacy of the services provided under the arrangement.</li> </ul> </li> <li>(e) the investment firm must have a comprehensive exit strategy, including where appropriate and proportionate taking into account the nature of the function subject to the outsourcing, partial exit and step-in clauses, and contingency plans;</li> <li>(f) the investment firm, including its compliance function and internal audit function (if any), should have complete access to its data; such access should also be provided to its external auditors (if any);</li> </ul> |   |
| <p style="text-align: center;"><b>Guideline 7</b></p> <p><b>An outsourcing institution should manage the risks associated with its outsourcing arrangements.</b></p> <p>1. Compliance with this Standard should include an ongoing assessment by the outsourcing institution of the operational risks and the concentration risk associated with all its outsourcing arrangements. An outsourcing institution should inform its supervisory</p>  | <p><b>Box 4 - Extracts from § 8</b></p> <ul style="list-style-type: none"> <li>(c) the investment firm must retain the required expertise to effectively supervise the outsourced functions and manage the risks associated with the outsourcing; senior management should take appropriate action if cause for concern arises;</li> <li>(f) the investment firm, including its compliance function and internal audit function (if any), should have complete</li> </ul>  | <p><b>Article 14(2) (Conditions for outsourcing critical or important operational functions or investment services or activities)</b></p> <p>Member States shall require investment firms to exercise due skill, care and diligence when entering into, managing or terminating any arrangement for the outsourcing to a service provider of critical or important operational functions or of any investment services or activities. Investment firms shall in particular take the necessary</p> |

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| <p>authority of any material development.</p>   | <p>access to its data; such access should also be provided to its external auditors (if any);</p>   | <p>steps to ensure that the following conditions are satisfied:<br/>(...)<br/>(c) the service provider must properly supervise the carrying out of the outsourced functions, and adequately manage the risks associated with the outsourcing;<br/>(d) appropriate action must be taken if it appears that the service provider may not be carrying out the functions effectively and in compliance with applicable laws and regulatory requirements;<br/>(e) the investment firm must retain the necessary expertise to supervise the outsourced functions effectively and manage the risks associated with the outsourcing and must supervise those functions and manage those risks;</p> |
| <p style="text-align: center;"><b>Guideline 8</b></p> <p><b>All outsourcing arrangements should be subject to a formal and comprehensive contract. The outsourcing contract should oblige the outsourcing service provider to protect confidential information.</b></p> <ol style="list-style-type: none"> <li>1. Any outsourcing arrangement should be based on a clear written contract.</li> <li>2. An outsourcing institution should make sure that the written contract takes account of the following (bearing in mind other specific national rules and legislation): <ol style="list-style-type: none"> <li>a. The operational activity that is to be outsourced should be clearly defined.</li> <li>b. The precise requirements concerning the performance of the service should be specified and documented, taking account of the objective of the outsourcing solution. The outsourcing service provider's ability to meet performance requirements in both quantitative and qualitative terms should be assessable in advance, including compliance with these Guidelines.</li> <li>c. The respective rights and obligations of the outsourcing institution and the outsourcing service provider should be precisely defined and specified. This should also serve to ensure compliance with laws and supervisory regulations and guidelines for the duration of the outsourcing arrangement.</li> <li>d. In order to underpin an effective policy for managing and monitoring the outsourced</li> </ol> </li> </ol> | <p style="text-align: center;"><b>BOX 4 – Extract from § 8</b></p> <p>(...)<br/>(d) the parties' respective responsibilities in relation to outsourcing must be clearly allocated in a written agreement; such agreement must also include, if applicable and where appropriate having regard to the function outsourced:</p> <ol style="list-style-type: none"> <li>(i) the law applicable to the contract;</li> <li>(ii) the relevant code of conduct and the compliance function in charge of monitoring its application;</li> <li>(iii) the obligation to protect confidential information;</li> <li>(iv) the obligation for the service provider to disclose material developments that may have an impact on the outsourced functions;</li> <li>(v) the contingency procedures;</li> <li>(vi) where permitted by national law and by the contract, the rules for subcontracting for the service provider;</li> <li>(vii) the termination rights of both parties; and</li> <li>(viii) the methods for measuring, and procedures for reporting, the quantitative and qualitative performance by the service provider, in order to enable the investment firm to assess the adequacy of the services provided under the arrangement</li> </ol> | <p style="text-align: center;"><b>Article 14(3)</b></p> <p>Member States shall require the respective rights and obligations of the investment firms and of the service provider to be clearly allocated and set out in a written agreement.</p>   |

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| <p>activities, the contract should include a termination and exit management clause, where proportionate and if deemed necessary, which allows the activities being provided by the outsourcing service provider to be transferred to another outsourcing service provider or to be reincorporated into the outsourcing institution.</p> <p>e. The contract should cover the protection of confidential information, banking secrecy and any other specific provisions relating to handling confidential information. Whenever information is subject to confidentiality rules at the level of the outsourcing institution at least the same level of confidentiality should be ensured by the service provider.</p> <p>f. The contract should ensure that the outsourcing service provider's performance is continuously monitored and assessed so that any necessary corrective measures can be taken promptly.</p> <p>g. The contract should include an obligation on the outsourcing service provider to allow the outsourcing institution's compliance and internal auditing departments complete access to its data and its external auditors full and unrestricted rights of inspection and auditing of data.</p> <p>h. The contract should include an obligation on the outsourcing service provider to allow direct access by the outsourcing institution's supervisory authority to relevant data and its premises as required.</p> <p>i. The contract should include an obligation on the outsourcing service provider to immediately inform the outsourcing institution, or the supervisory authority directly, of any material changes in circumstances which could have a material impact on the continuing provisions of services. This may require obtaining consents from affected parties such as the parent company and relevant home supervisory authority.</p> <p>j. The outsourcing contract shall contain provisions allowing the outsourcing institution to cancel the contract by contractual notice of dismissal or extraordinary notice of cancellation if so required by the supervisory authority.</p> <p>3. When drafting the contract the outsourcing institution should bear in mind that the level of monitoring,</p> |  |  |
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| <p>assessment, inspection and auditing required by the contract should be proportionate to the risks involved and the size and complexity of the outsourced activity.</p>   |  |   |
| <p align="center"><b>Guideline 9</b></p> <p><b>In managing its relationship with an outsourcing service provider an outsourcing institution should ensure that a written agreement on the responsibilities of both parties and a quality description is put in place.</b></p> <ol style="list-style-type: none"> <li>1. A written agreement should normally contain a mixture of quantitative and qualitative performance targets, to enable an outsourcing institution to assess the adequacy of service provision.</li> <li>2. An outsourcing institution should also consider the need to evaluate the performance of its outsourcing service provider using mechanisms such as service delivery reports, self-certification or independent review by the outsourcing institution's, or the outsourcing service provider's, internal and/or external auditors.</li> <li>3. An outsourcing institution should be prepared to take remedial action if the outsourcing service provider's performance is inadequate.</li> </ol> | <p><b>Box 4 – Extract from § 8</b></p> <p>d) the parties' respective responsibilities in relation to outsourcing must be clearly allocated in a written agreement; such agreement must also include, if applicable and where appropriate having regard to the function outsourced:</p> <p>(...)</p> <p>(viii) the methods for measuring, and procedures for reporting, the quantitative and qualitative performance by the service provider, in order to enable the investment firm to assess the adequacy of the services provided under the arrangement.</p> | <p><b>Article 14(2)</b></p> <p>2. (...) Investment firm shall in particular take the necessary steps to ensure that the following conditions are satisfied:</p> <p>(...)</p> <p>(b) the service provider must carry out the outsourced services effectively, and to this end the firm must establish methods for assessing the standard of performance of the service provider;</p> <p>3. Member States shall require the respective rights and obligations of the investment firms and of the service provider to be clearly allocated and set out in a written agreement.</p> |
| <p align="center"><b>Guideline 10</b></p> <p><b>10.1 Supervisory authorities should take account of the risks associated with "chain" outsourcing.</b></p>  | <p><b>BOX 4 – Extract from § 8</b></p> <p>(d) the parties' respective responsibilities in relation to outsourcing must be clearly allocated in a written agreement; such agreement must also include, if applicable and where appropriate having regard to the function outsourced:</p> <p>(...)</p> <p>(vi) where permitted by national law and by the contract, the rules for subcontracting for the service provider;</p>   |   |
| <p><b>10.2 The supervisory authority should agree to chain outsourcing only if the sub-contractor will also fully comply with the obligations existing between the outsourcing institution and the outsourcing service provider, including obligations incurred in favour of the supervisory authority.</b></p>   |  |   |
| <p><b>10.3 The outsourcing institution should take appropriate steps to address the risk of any weakness or failure in the provision of the subcontracted activities having a significant effect on the outsourcing service provider's ability to meet its responsibilities under the outsourcing</b></p>   |  |   |

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| <p><b>agreement.</b></p> <ol style="list-style-type: none"> <li>1. The sub-outsourcing of outsourced activities and functions to third parties (sub-contractors) should be treated by the outsourcing institution like a primary outsourcing measure. Compliance with these conditions should be ensured contractually, for example by a clause in the outsourcing contract requiring the prior consent of the outsourcing institution to the possibility and the modalities of sub-outsourcing.</li> <li>2. The outsourcing institution should ensure that the outsourcing service provider agrees that the contractual terms agreed with the sub-contractor will always conform, or at least not be contradictory, to the provisions of the agreement with the outsourcing institution.</li> </ol>  |  |  |
| <p><b>Part 3: Guidelines on outsourcing addressed to supervisory authorities</b></p> <p style="text-align: center;"><b>Guideline 11</b></p> <p><b>Supervisory authorities should require that the outsourcing institution has established supervisory authority access to relevant data held by the outsourcing service provider and, where provided for by national law, the right for the supervisory authority to conduct on-site inspections at an outsourcing service provider's premises.</b></p> <ol style="list-style-type: none"> <li>1. Supervisory authorities should aim to be satisfied that outsourcing institutions ensure that their outsourcing contracts with outsourcing service providers grant the supervisory authority the rights to information and, where provided for by national law, to inspection, admittance and access (including access to databases) as well as the right to give directions or instructions, which the supervisory authority needs to exercise its supervisory functions.</li> <li>2. Supervisory authorities should encourage outsourcing institutions to ensure that information may also be made available to the supervisory authority by the outsourcing service provider's external auditor.</li> <li>3. Supervisory authorities should aim to ensure that their powers to issue orders or instructions to the outsourcing institution can be reliably enforced, without being compromised by instructions issued to the outsourcing service provider by other bodies, so as to ensure the orderly performance of the outsourced activities.</li> </ol> | <p><b>Requirement on investment firm</b></p> <p><b>BOX 4 – Extract from § 8</b></p> <p>(g) the investment firm must ensure that the terms of the contract with the service provider require the latter to deal in a open and cooperative way with the competent authorities in the discharge of their functions under the Directive, including permitting access to the relevant data and its business premises, and that the competent authorities can exercise those rights.</p> | <p><b>Article 14(2)</b></p> <p>Member States shall require investment firms to exercise due skill, care and diligence when entering into, managing or terminating any arrangement for the outsourcing to a service provider of critical or important operational functions or of any investment services or activities. Investment firms shall in particular take the necessary steps to ensure that the following conditions are satisfied:</p> <p>(...)</p> <ol style="list-style-type: none"> <li>(h) the service provider must cooperate with the competent authorities of the investment firm in connection with the outsourced activities;</li> <li>(i) the investment firm, its auditors and the relevant competent authorities must have effective access to data related to the outsourced activities, as well as to the business premises of the service provider; and the competent authorities must be able to exercise those rights of access;</li> </ol> |



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| <p>4. The supervisory authorities should aim to ensure that they can obtain detailed information about any outsourcing processes which might undermine the stability of the consolidated group whose overall supervision is, ultimately, their responsibility.</p> <p>5. In the case of outsourcing to service providers abroad, the outsourcing institution should be responsible for ensuring that the supervisory authority can exercise its information gathering rights, including its right to demand documents and audits, and, compatibly with the overall legal framework its inspection rights.</p> <p>6. The requirement to cancel the outsourcing contract (under Guideline 8.2(j) should be properly justified by the supervisor on the basis of non-compliance with the provisions of these guidelines, in particular of those with regard to the safeguarding of rights of supervision and enforcement.</p> <p>7. The outsourcing institution may – prior to outsourcing – consider in consultation with the supervisory authority what alternative measures could adequately mitigate the risks involved.</p> |   |  |
| <p style="text-align: center;"><b>Guideline 12</b></p> <p><b>Supervisory authorities should take account of concentration risk.</b></p> <p>1. Supervisory authorities should seek to identify any concentration risk on a sectoral level and seek to monitor these risks at a systemic level.</p>   | <p><b>Box 4 – Extract from § 8</b></p> <p>(b) the investment firm must ensure that the service provider has the ability and capacity to perform the outsourced functions reliably and professionally. To that end, the investment firm must evaluate the service provider and its services at the start and during the life cycle of the outsourcing. In performing this evaluation, the matters of which the investment firm should take particular account include where relevant, whether the service provider is regulated, to what extent and by whom, including whether the provision of the outsourced functions is subject to specific regulation or supervision, <b>and the risk that the requested services are not available due to the number of other persons using the same service provider;</b></p> |  |