



**BANGKO SENTRAL NG PILIPINAS**

OFFICE OF THE GOVERNOR

**CIRCULAR NO. 764**

Series of 2012

**Subject: Revised Outsourcing Framework for Non-Bank Financial Institutions**

The Monetary Board, in its Resolution No. 1179 dated 19 July 2012, approved the revisions to the outsourcing framework of non-bank financial institutions, amending the Manual of Regulations for Non-Bank Financial Institutions (MORNBFII) particularly Section 4162Q (2008 – 4190Q) for Quasi-Banks, Section 4190S for NSSLAs, Section 4190P for Pawnshops and Section 4190N for Other NBFIs, Trust Entities, Subsidiaries and Affiliates of Banks and Quasi-Banks.

1. Section 4162Q [(2008 – 4190Q) Duties and Responsibilities of Quasi-Banks and their Directors/Officers in All Cases of Outsourcing of Quasi-Banking Functions] is re-titled and amended to read as follows:

Section 4162Q (2008 – 4190Q) **Guidelines on Outsourcing**. The rules on outsourcing of banking functions as shown in Appendix Q-37 shall be adopted insofar as they are applicable to QBs.

2. Subsection § 4406Q.9 Outsourcing Services in Trust Departments is amended to read as follows:

Subsection § 4406Q.9 **Outsourcing Services in Trust Departments**. The rules on outsourcing of banking functions as shown in Appendix Q-37 shall be adopted insofar as they are applicable to trust departments of QBs performing trust and other fiduciary business and investment management activities.

3. Subsection § 4701Q.13 Outsourcing of Internet and Mobile Electronic Services is amended to read as follows:

Subsection § 4701Q.13 **Outsourcing of Internet and Mobile Electronic Services**. The rules on outsourcing of banking functions as shown in Appendix Q-37 shall be adopted insofar as they are applicable to quasi-banks' outsourcing of internet and mobile electronic services.

4. Section 4190S Duties and Responsibilities of NSSLAs and their Directors/Officers in All Cases of Outsourcing of NSSLA Functions is re-titled and amended to read as follows:

Section 4190S **Guidelines on Outsourcing.** The rules on outsourcing of banking functions as shown in Appendix Q-37 shall be adopted insofar as they are applicable to NSSLAs.

5. Section 4190P Duties and Responsibilities of Pawnshops and their Directors/Officers in All Cases of Outsourcing of Pawnshop Functions is re-titled and amended to read as follows:

Section 4190P **Guidelines on Outsourcing.** The rules on outsourcing of banking functions as shown in Appendix Q-37 shall be adopted insofar as they are applicable to Pawnshops.

6. Section 4190N Duties and Responsibilities of Non-Bank Financial Institutions and their Directors/Officers in All Cases of Outsourcing of Non-Bank Financial Institutions is re-titled and amended to read as follows:

Section 4190N **Guidelines on Outsourcing.** The rules on outsourcing of banking functions as shown in Appendix Q-37 shall be adopted insofar as they are applicable to FIs.

7. Appendix 37 of the MORNBFIs is re-titled as Revised Outsourcing Framework for Banks and amended to read as shown in the *Annex A*.

This Circular shall take effect fifteen (15) calendar days following its publication either in the Official Gazette or any newspaper of general circulation.

**FOR THE MONETARY BOARD:**

  
**AMANDO M. TETANGCO, JR.**  
Governor

3 August 2012

**REVISED OUTSOURCING FRAMEWORK FOR BANKS**  
**(Appendix to Section 4162Q (2008-4192Q, 4190S, 4190P, 4190N))**

1. Section X162 of the MORB [(2008 – X169) Duties and Responsibilities of Banks and their Directors/Officers in All Cases of Outsourcing of Banking Functions] is re-titled and amended to reflect a statement of principle which shall read as follows:

Section X162 ***Statement of Principle on Outsourcing***. An institution may outsource banking support and marketing activities subject to the provisions set forth below. Accordingly, an institution is exposed to operational risks as a result of outsourcing. As such, an institution that avails of outsourcing should have in place appropriate mechanisms to ensure the effective management of attendant risks.

2. The previous Section X162 of the MORB shall be renumbered as Subsection § X162.1 and amended to read as follows:

Subsection § X162.1 ***Governance in All Cases of Outsourcing of Banking Functions***. When outsourcing is allowed by law, a bank shall:

- a. Be responsible for the performance of the outsourced activity in the same manner and to the same extent as if it was performing directly the said activity;
- b. Comply with all laws and regulations applicable in the Philippines including labor laws and those governing the banking activities/services performed by the qualified service providers on the bank's behalf;
- c. Monitor and review on an ongoing basis the performance of the service providers undertaking the outsourced activity and/or service; and
- d. Update as necessary its assessment of the extent of the materiality of its outsourcing arrangements vis-à-vis the adequacy of its risk management system.

3. The previous Subsection § X162.1 of the MORB [(2008 – X169.1) Prohibition against outsourcing certain banking functions] shall be re-numbered as Subsection § X162.2. The previous Subsection § X162.2 (2008 – X169.2) on Outsourcing of Information Technology Systems/Processes is amended and transferred to the Appendix of Section X162 of the MORB on relevant documentations. The new Subsection § X162.2 is amended to read as follows:

Subsection § X162.2 ***Prohibition against outsourcing of inherent banking functions.***

No bank shall outsource inherent bank functions such as:

1. Services normally associated with placement of deposits and withdrawals including the recognition based on recording of movements in the deposit accounts;
  2. Granting of loans and extension of other credit exposures;
  3. Position-taking and market risk-taking activities;
  4. Managing of risk exposures; and
  5. Strategic decision-making.
4. The previous Subsection § X162.3 [(2008 – X169.3) – Outsourcing of Other Banking Functions] is deleted. The new Subsection § X162.3 of the MORB shall contain the definition of outsourcing and shall read as follows:

Subsection § X162.3 ***Definition.*** Outsourcing shall refer to any contractual arrangement between a bank and a qualified service provider for the latter to perform designated activities on a continuing basis on behalf of the bank.

5. The new Subsection § X162.4 of the MORB shall focus on the responsibility of the bank to manage the operational risks that arise from outsourcing. It shall read as follows:

Subsection § X162.4 ***Managing Outsourcing-Related Risks.*** No bank may outsource banking activities unless it has in place the appropriate processes, procedures, and information system that can adequately identify, monitor and mitigate operational risks that are borne by the bank as a result of its outsourcing activities.

A bank shall determine the materiality of its outsourcing arrangements when establishing guidelines, processes and controls in managing outsourcing risks. An outsourcing arrangement is considered material if the activity, when disrupted, has the potential to significantly impact the bank's business operations, reputation, profitability or regulatory responsibilities. A bank may take into consideration the following factors in determining the materiality of its outsourcing arrangements:

- i. Importance of the activity to be outsourced and the potential impact of outsourcing on earnings, solvency, liquidity, funding and capital and risk profile;

- ii. Consideration on the bank's reputation and ability to achieve its objectives, strategy and plans, should the service provider fail to perform the services;
- iii. Aggregate exposure to a particular service provider in cases where the bank outsources various functions to the same service provider;
- iv. Ability to maintain appropriate internal controls and meet regulatory requirements, if there were operational problems faced by the service provider; and
- v. Exposure to risk of confidentiality, integrity and availability of customer and bank data.

After due evaluation of a bank's risk management processes with respect to outsourcing, the BSP may require the bank to terminate, modify, make alternative arrangements or re-integrate the activity into the bank, as may be necessary, in cases where the risk infrastructure is deemed inadequate for purposes of managing outsourcing-related risks.

6. The new Subsection § X162.5 shall read as follows:

**Subsection § X162.5 *Authority to Outsource.*** Only those banks with a CAMELS composite rating of at least "3" and a Management Rating of not lower than "3" shall be allowed to outsource designated activities without prior BSP approval. Otherwise, the bank must secure prior approval from the appropriate supervising department of the BSP whose evaluation will be based on the bank's ability to manage risks attendant to outsourcing.

7. The new Subsection § X162.6 shall read as follows:

**Subsection § X162.6 *Documentations.*** The bank should maintain necessary documentation to show that outsourcing arrangements are properly reviewed and the appropriate due diligence has been undertaken prior to implementation.

The bank shall keep in its file the documents shown in *Annex A of Appendix 37* and the same shall be made available to authorized representatives of the BSP for inspection.

8. Subsections § X162.11 (2008 – X169.11) and § X162.12 (2008 – X169.12) of the MORB are consolidated, re-titled and renumbered as Subsection § X162.7 and amended to read as follows:

**Subsection § X162.7 *Intra-group Outsourcing.*** The guidelines and requirements of outsourcing to third-party service providers shall be observed when outsourcing within a business group including its head office, another branch or related company.

When the bank is the service provider, the bank may only render services it performs in the ordinary course of its banking business, provided that: (i) the service is rendered to subsidiaries, affiliates and companies related to it by at least 5% common ownership; or (ii) the service is rendered to its own depositors on account of the bank being a depository.

The bank, acting as a service provider within its group, shall uphold the following:

- a. Confidentiality of deposits and investments in government bonds as defined under Republic Act No. 1405, as amended; and
- b. Prohibition on cross-selling except as allowed under applicable regulations.

9. The new Subsection § X162.8 shall read as follows:

**Subsection § X162.8 *Offshore Outsourcing.*** Offshore outsourcing exists when the service provider is located outside the country. Subsection X162.7 of the MORB on Intra-Group Outsourcing likewise applies in cases of offshore outsourcing. In addition, offshore outsourcing of the bank's domestic operations is permitted only when the service provider operates in jurisdictions which uphold confidentiality.

When the service provider is located in other countries, the bank should take into account and closely monitor, on continuing basis, government policies and other conditions in countries where the service provider is based during risk assessment process. The bank shall also develop appropriate contingency and exit strategies.

The BSP examiners shall be given access to the service provider and those relating to the outsourced domestic operations of the bank. Such access may be fulfilled by on-site examination through coordination with host authorities, if necessary. The domestic branch of foreign bank shall be principally liable in cases where the clients are prejudiced due to errors, omissions and frauds of the service provider located offshore.

The BSP may require the bank to terminate, modify, make alternative outsourcing arrangements or re-integrate the outsourced activity into the bank, as may be necessary, if confidentiality of customer information, effective

customer redress mechanisms or the ability of the BSP to carry out its supervisory functions cannot be assured.

10. The previous Subsection § X162.4 (2008 – X169.4) of the MORB on ***Service Providers*** is renumbered as the new Subsection § X162.9. It shall be amended to read as follows:

Subsection X162.9 ***Service Providers***. The bank shall carry out due diligence in selecting service providers. It must ensure the integrity, technical expertise, operational capability, financial capacity and suitability of the service provider to perform the outsourced activity. In cases where the clients are prejudiced due to errors, omissions and frauds by the service provider, the bank shall be liable in providing the appropriate remedies as may be allowed by laws or regulations, without prejudice to recourse by the bank to the service provider.

11. The previous Subsection § X162.5 on Review of subsisting outsourcing contracts is renumbered as Subsection § X162.10 and re-titled as Transitory Provision. It is amended to read as follows:

Subsection X162.10. ***Transitory Provision***. All outsourcing agreements must be aligned with the provisions of Section X162 of the MORB. Existing outsourcing agreements which are not in accordance with this circular will not be unwound. However, it must comply with the requirements provided herein upon renewal of the agreements.

12. The previous Subsection § X162.19 on ***Penalties*** is re-numbered as Subsection § X162.11.

**Appendix to Section X162 of the MORB (2008 – X169) on the  
Revised Outsourcing Framework for Banks**

1. A comprehensive policy on outsourcing duly approved by the board of directors of the bank.
2. Service level agreement or contract between the bank and the service provider, which shall, at a minimum, include all of the following:
  - a. Complete description of the work to be performed or services to be provided;
  - b. Fee structure;
  - c. Provisions regarding on-line communication availability, transmission line security, and transaction authentication (*applicable to IT outsourcing*);
  - d. Responsibilities regarding hardware, software and infrastructure upgrades (*applicable to IT outsourcing*);
  - e. Provisions governing amendment and pretermination of contract;
  - f. Mandatory notification by the service provider of all systems changes that will affect the bank (*applicable to IT outsourcing*);
  - g. Details of all security procedures and standards (*applicable to IT outsourcing*);
  - h. Responsibility, fines, penalties and accountability of the service provider for errors, omissions and frauds;
  - i. Confidentiality clause covering all data and information; solidary liability of service provider and bank for any violation of R.A. No. 1405, (the Bank Deposits Secrecy Law) actions that the bank may take against the service provider for breach of confidentiality or any form of disclosure of confidential information; and the applicable penalties;
  - j. Segregation of the data of the bank from that of the service provider and its other clients;
  - k. Disaster recovery/business continuity contingency plans and procedures;
  - l. Adequate insurance for fidelity and fire liability (*applicable to IT outsourcing*);
  - m. Ownership/maintenance of the computer hardware, software (program source code), user and system documentation, master and transaction data files (*applicable to IT outsourcing*);
  - n. Guarantee that the service provider will provide necessary levels of transition assistance if the bank decides to convert to other service providers or other arrangements;
  - o. Access to the financial information of the service provider;
  - p. Access of internal and external auditors to information regarding the outsourced activities/services which they need to fulfill their respective responsibilities;
  - q. Access of BSP to the operations of the service provider in order to review the same in relation to the outsourced activities/services;
  - r. Provision which requires the service provider to immediately take the necessary corrective measures to satisfy the findings and recommendations of BSP examiners and those of the internal and/or external auditors of the bank and/or the service provider;



**Annex A of Appendix 37**

- s. Remedies for the bank in the event of change of ownership, assignment, attachment of assets, insolvency, or receivership of the service provider; and
  - t. Provision allowing the bank to cancel the contract by contractual notice of dismissal or extraordinary notice of cancellation if so required by the BSP.
3. Secretary's certificate on the minutes of meeting of the board of directors of the bank (or a local/regional management committee, in case of foreign banks), explicitly approving the activity to be outsourced, the determination of whether an outsourcing arrangement is considered material or non-material and the specific service provider with which the bank is entering into an outsourcing contract;
  4. Profile of the selected service provider; and
  5. A central record of all outsourcing arrangements which shall be periodically updated and shall form part of the corporate governance reviews undertaken by the bank.