



BANGKO SENTRAL NG PILIPINAS

OFFICE OF THE DEPUTY GOVERNOR FINANCIAL SUPERVISION SECTOR

MEMORANDUM NO. M-2022-046

To : **ALL BSP-SUPERVISED FINANCIAL INSTITUTIONS (BSFIs)**

Subject : **Frequently Asked Questions on the Amendments to the Regulations on Outsourcing and IT Risk Management**

The BSP issues the attached Frequently Asked Questions (FAQ) on Circular No. 1137 on the Amendments to the Regulations on Outsourcing and IT Risk Management (Annex A) to provide additional guidance and clarification on the implementation of the said Circular. This document covers the following:

1. Conduct of materiality assessment and maintenance of outsourcing register;
2. Intra-group and offshore outsourcing, and subcontracting arrangements;
3. Cloud outsourcing;
4. Additional outsourcing activity;
5. IT Outsourcing Questionnaire; and
6. Timeline on the submission of documentary requirements.

For information and guidance.

A handwritten signature in black ink, appearing to read 'Chuchi G. Fonacier', is positioned above the printed name.

Digitally signed by
Chuchi G. Fonacier
Date: 2022.10.27
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CHUCHI G. FONACIER
Deputy Governor

27 October 2022

**FREQUENTLY ASKED QUESTIONS (FAQ) ON THE
AMENDMENTS TO REGULATIONS ON OUTSOURCING
AND IT RISK MANAGEMENT
(Circular No. 1137 dated 18 February 2022)**

Introduction

As the BSP recognizes technology developments in the industry and their impact on the business operations and initiatives of BSP-supervised financial institutions (BSFIs), the Monetary Board (MB) approved the Amendments to the Regulations on Outsourcing and Information Technology Risk Management issued under Circular No. 1137. The Circular applies a risk-based approach on technology outsourcing consistent with international practices and in line with recent industry developments.

The following responses to the FAQs on Circular No. 1137 aim to provide guidance and facilitate implementation of the said issuance:

A. Conduct of materiality assessment and maintenance of outsourcing register

1. *Is the maintenance of outsourcing register, as provided in Appendix 103/Q-36, applicable only for material outsourcing arrangements? In relation to this, are BSFIs required to conduct materiality assessment for existing outsourcing arrangements?*

No, the outsourcing register should include all outsourcing arrangements, both material and non-material. The required minimum information for the outsourcing register is indicated in Appendix 103 Section A of subject Circular.

Meanwhile, BSFIs are expected to conduct materiality assessment for both new and existing outsourcing arrangements. BSFIs may initially identify materiality of existing outsourcing engagements based on current company policies. For instance, existing outsourcing contracts that are subject to annual (or more frequent) reviews may be *initially* assessed as material while those subject to less frequent reviews may be *initially* assessed as non-material.

Nonetheless, BSFIs should update the corresponding outsourcing and vendor management policies taking into account the provisions of Circular No. 1137, and subsequently undertake a more comprehensive materiality assessment of ALL outsourcing arrangements based on the revised policies and procedures.

2. *Since there are no defined weights/scores and methodology in determining the level of materiality of outsourced activities/arrangements based on the factors enumerated in the Circular, are BSFIs allowed to develop their own materiality scoring/rating system?*

Yes, BSFIs may develop their own rating/scoring methodology to aid in the assessment of overall materiality of outsourcing arrangements, based on factors enumerated in Annex A of the Circular. This, however, does not preclude the BSP from evaluating the soundness of the Bank's internal rating/scoring methodology.

B. Intra-group and offshore outsourcing, and subcontracting arrangements

1. *The Circular has provided definitions and guidelines related to intra-group outsourcing and offshore outsourcing. How should BSFIs classify intra-group outsourced activity provided by offshore-based unit/group?*

If an outsourcing activity falls within the definition of both intra-group and offshore outsourcing, as provided in Circular No. 1137, then said outsourcing arrangement is considered as both an intragroup and offshore outsourcing service. Hence, the outsourcing activity shall not require prior BSP approval once relevant intra-group or offshore outsourcing conditions are met. In any other case, the general guidelines and requirement on outsourcing shall apply.

2. *In relation to the guidelines on intra-group outsourcing arrangements, in case the BSFI is unable to meet all the following conditions, namely, (i) the services rendered are performed in the ordinary course of business; (ii) the service provider is likewise a regulated financial institution; and (iii) the service is rendered to subsidiaries, affiliates and companies related to the service provider through common ownership, will the BSFI need to seek BSP approval prior to implementation of said outsourcing arrangement?*

If the intra-group outsourcing activity does not meet ALL the conditions provided in the Circular, the general outsourcing guidelines and requirements shall apply. This includes, among others, the assessment/identification of the level of materiality and SAFr¹ rating to determine whether the outsourcing activity requires prior BSP approval.

3. *Please confirm whether an intra-group outsourcing arrangement which meets the following conditions, namely, (i) the services rendered are performed in the ordinary course of business; (ii) the service provider is likewise a regulated financial institution; and (iii) the service is rendered to subsidiaries, affiliates and companies related to the service provider through common ownership, does not require prior BSP approval regardless of SAFr rating and level of materiality of outsourced activity.*

If an intragroup outsourcing activity meets all three (3) conditions provided in the Circular, prior BSP approval is not required. However, BSFIs are still expected to assess the materiality of said outsourcing engagement. If deemed material, regardless of the BSFI's SAFr rating, the requirements under Section B of Appendix 103/Q-36 shall apply (For material outsourcing that DO NOT REQUIRE prior Bangko Sentral approval).

¹ Supervisory Assessment Framework (SAFr)

4. *Prior to the issuance of Circular No. 1137, the intra-group outsourcing covers the relationship between the head office and its branch. However, the current amendments on intra-group outsourcing regulations exclude reference to head office-branch relationship. Does it follow that support services rendered by the head office to its foreign branch are no longer considered as outsourcing under the existing provisions?*

Branch operations are technically extensions of the head office, thus, the services rendered by the head office to its foreign branch/es shall not be considered as outsourcing activities. Nonetheless, the branch of the foreign bank is expected to monitor and evaluate the quality/level of services rendered by its head office, as guided by the bank's service level agreement between concerned units.

5. *The guidelines excluded "branch of foreign banks" when referring to intra-group outsourcing. Does it imply that the statement "services rendered to subsidiaries, affiliates and companies related to the service provider through common ownership" are also applicable to branches of foreign banks?*

Yes, in cases wherein the foreign bank branch enters into an outsourcing arrangement with a service provider/entity within the common ownership group, the guidelines on intra-group outsourcing shall apply.

6. *For subcontracting agreements, please confirm whether prior BSP approval of the outsourcing agreement between the BSFI acting as the intra-group service provider and the subcontractor will still take into consideration the level of materiality and the BSFI's SAFr rating. What if the intra-group service provider is not a BSFI?*

Yes, the general outsourcing guidelines and requirements shall apply to BSFIs acting as intra-group service provider in relation to their subcontracting arrangement. This means that the determination on whether prior BSP approval is needed shall be determined by the BSFI's SAFr rating and the level of materiality of the outsourced activity (subcontracting services).

On the other hand, if the intra-group service provider entering into a subcontracting agreement is not a BSFI, then the BSFI (recipient of the outsourcing service) shall follow the general guidelines and requirements on outsourcing as provided in Circular No. 1137, including proper disclosure of subcontracting arrangements to the BSP.

7. *In case the BSFI's third party service provider enters into an outsourcing arrangement (e.g., cloud hosting services) with another service provider (subcontracting), is this agreement expected to conform with the provisions set forth in the circular?*

While existing regulations do not prohibit subcontracting arrangements, Section 3.3 of Appendix 78 of the Manual of Regulations for Banks (MORB) clearly states that,

"Some service providers may contract with third-parties in providing IT services to the BSFI. The extent to which subcontractors perform additional services should be limited to peripheral or support functions while the core services should rest with the main service provider. The BSFI should retain the ability to maintain similar control over its outsourcing risks when a service provider uses subcontractors in the course of rendering the IT-related services. Agreements should have clauses setting out the rules and limitations on subcontracting. To provide accountability, it may be beneficial for the BSFI to include a provision specifying that the contracting service provider shall remain fully responsible with respect to parts of the services which were further outsourced to subcontractors. It should also consider including notification and approval requirements regarding changes to the service provider's significant subcontractors."

C. Cloud outsourcing

1. *With the deletion of the section on cloud outsourcing in Appendix 78, is cloud outsourcing still considered as an outsourcing arrangement? If yes, is it necessary to distinguish various types of cloud outsourcing arrangements when entering into such agreement? Further, are BSFIs expected to include the type of cloud hosting services in assessing the level of materiality?*

Yes, cloud outsourcing arrangements are still considered as IT outsourcing; hence, these are subject to the provisions of Circular No. 1137. In case a BSFI enters into such agreement, it should identify the type of cloud hosting services to allow the BSFI to manage risks accordingly. Further, the IT Outsourcing Questionnaire (Section A – Overview of the Outsourced Activities and Service Providers) also requires information on activities, operations, and services to be outsourced, which basically pertains to the type of cloud hosting arrangements, if applicable.

In terms of materiality assessment, the BSFIs are not required to include cloud service-specific factors (e.g., type of cloud hosting services) in addition to the five (5) materiality factors as provided in the Circular, but may opt to do so if deemed necessary.

2. *Please confirm whether the deletion of Section 4 of Appendix 78 is equivalent to lifting of restrictions on the use of public cloud for core operations.*

Yes, BSFIs may engage in any type of cloud outsourcing services, whether for core or non-core operations, subject to the guidelines and requirements of the outsourcing circular.

3. *Since BSFIs incur costs in the engagement of SOC 2 Type 2 Audit, will the BSP allow other external audit report and/or service provider's internal audit as acceptable alternative procedures/documentary requirements?*

In case a SOC 2 Type 2 Report for the cloud service provider is not available, BSFIs may submit alternative report/s so long as the review was conducted by an independent external party.

D. Additional outsourcing activity

1. *In case the BSP issues approval of outsourcing arrangement (e.g. cloud hosting) between the BSFI and service provider, will such approval extend to subsequent additional services that will be offered by the same service provider to the BSFI?*

If a material outsourcing arrangement requires prior BSP approval, such approval shall only pertain to the activities/services at the time of application and evaluation. Hence, it does not cover additional services to be availed in the future. Subsequent changes to any type of outsourcing arrangement of BSFIs with SAFr rating of below "3" shall require prior BSP approval, under the following circumstances:

- a. Changes in existing material outsourcing arrangements that have significant impact in the delivery of outsourcing services, business operations, reputation and profitability; and
- b. Changes in existing outsourcing arrangements resulting in the reclassification of the arrangements as material such as, but not limited to those affecting the nature, scope, and complexity of systems and processes.

In case a BSFI with a SAFr rating of at least "3" takes on subsequent changes, as mentioned in items a and b above, said arrangements shall not require prior BSP approval, but are subject to submission of documents, as provided in the appendix of the Circular.

E. IT Outsourcing Questionnaire

1. *As provided in Annexes 103-1 and 103-2, the IT outsourcing questionnaires must undergo review and sign-off by C-suite executives prior to submission to the BSP. In the event that C-suite executives are based at the regional offices, as in the case of foreign bank branches, who are required to conduct self-assessment review and sign-off?*

Questionnaires must be reviewed and signed off by C-suite executive with direct understanding of the outsourced activities and their attendant risks. In case the C-suite executives are based at the regional offices, questionnaires may be reviewed and signed off by an officer of equivalent rank (e.g., Country Manager) as long as said officer has proper knowledge and sufficient understanding of the outsourced activity and related risks.

2. *For Appendix 103-2 (IT Outsourcing Questionnaire for Technology Service Provider), please confirm that while the information will be obtained from the*

Technology Service Provider (TSP), the review and sign-off will be performed by the C-suite executive of the BSFI.

Yes, sign-off and review for the IT Outsourcing Questionnaire for TSPs will be the responsibility of the BSFI's C-suite executive.

F. Timeline on the submission of documentary requirements

- 1. Will the BSP still require submission of additional documentary requirements? The submission of additional requirements becomes of particular concern in case project schedules are subject to tight timelines, hence, on-time implementation of outsourcing arrangements is critical in the achievement of business requirements/objectives.*

The BSP may require submission of additional information/documents to address deficiencies in submitted documents or to obtain further clarification, as may be necessary. In view of this, BSFIs are strongly encouraged to ensure timely submission of complete and accurate information/documents to avoid potential delays in planned activities.