

# MAS publishes revised Guidelines on Outsourcing

The Monetary Authority of Singapore (MAS) has published the revised Guidelines on Outsourcing (Guidelines), which replace the previous Guidelines on Outsourcing and IT Outsourcing Circular published by MAS. The Guidelines provide institutions with guidance on sound practices for risk management of their outsourcing arrangements.

**We set out in this briefing a high-level overview of the Guidelines and the key differences between the revised Guidelines and the previous Guidelines.**

## Scope and application of Guidelines

MAS first published the Guidelines in October 2004, which were updated in July 2005. In September 2014, MAS released two consultation papers relating to outsourcing arrangements. The first related to proposed revisions to the Guidelines and the second related to a proposed new notice on outsourcing.

MAS has now published its responses to the first consultation paper, as well as the revised Guidelines. It has not yet published its responses to the second consultation paper on the proposed notice, but has advised that it intends to issue the notice at a later date and will engage the industry prior to this, if necessary.

The revised Guidelines apply from 27 July 2016 to any "institution" that has entered into an "outsourcing arrangement", or that is planning to outsource its business activities to a "service provider".

The revised Guidelines define an "outsourcing arrangement" as an arrangement in which a service provider provides the institution with a service that may currently or potentially be performed by the institution itself and which includes the following characteristics: (a) the institution is dependent on the service on an ongoing basis; and (b) the service is integral to the provision of a financial service by the institution or the service is provided to the market by the service provider in the name of the institution.

Notably, the new definition no longer specifically excludes services that involve the provision of a finished product. MAS has indicated that whether an arrangement would be deemed as outsourcing would depend on its characteristics as set out in the revised Guidelines. For instance, while the purchase of software is a finished product, an arrangement with a vendor to provide ongoing support to keep software updated and relevant could be regarded as outsourcing.

Further, the reference to it being prohibitive or costly to change service

provider has been removed from the definition as MAS has assessed that this characteristic is no longer relevant in determining whether an arrangement should be deemed as outsourcing.

The "Examples of Outsourcing Arrangements" in Annex 1 of the revised Guidelines have also been amended. Notably, the list of "Arrangements that are generally considered low-risk" in the previous Guidelines has been removed. This is because some of the activities are no longer considered low risk and MAS expects institutions to make their own risk assessment.

"Service provider" is defined broadly in the revised Guidelines to refer to any party which provides a service to the institution, including any entity within the institution's group, whether it is located in Singapore or elsewhere.

As with the previous Guidelines, the revised Guidelines are not legally binding, and MAS will review an institution's implementation of the Guidelines to assess the quality of its board and senior management

oversight and governance, internal controls and risk management.

The revised Guidelines have also introduced a requirement for an institution to maintain a register of all of its outsourcing arrangements (including its material outsourcing arrangements). Annex 3 of the revised Guidelines sets out the minimum information which the register should capture. The register is required to be submitted to MAS at least annually or upon request.

#### Expansion of scope of "institutions"

It should be noted that the scope of "institutions" to which the Guidelines apply has expanded to include "*any financial institution as defined in section 27A of the MAS Act*", which would include licensed money-changers, holders of stored value facilities, licensed trust companies, and any other person licensed, approved, registered or regulated by MAS under any written law. Notably, pursuant to limb (7) of Section 27A, this includes a person who is exempted from being licensed, approved, registered or regulated.

#### Service providers and sub-contractors

MAS has clarified in the revised Guidelines that an institution should ensure that services that it outsources (whether provided by a service provider or its sub-contractor) should continue to be managed as if the services were managed by the institution.

#### Singapore groups

Singapore-incorporated institutions are required to ensure that branches and corporations under their control observe the Guidelines through a group-wide outsourcing risk

management framework that complies with the Guidelines.

## Material outsourcing arrangements

#### Expanded definition of "material outsourcing arrangement"

The definition of "*material outsourcing arrangement*" has been amended in the revised Guidelines to mean an outsourcing arrangement that:

- in the event of a service failure or security breach, has the potential either to materially impact an institution's business operations, reputation or profitability, or its ability to manage risk and comply with applicable laws and regulations; or
- involves customer information and, in the event of any unauthorised access or disclosure, loss or theft of customer information, may have a material impact on an institution's customers.

Notably, detailed definitions of "customer information" and "customer" have been included in the revised Guidelines. Annex 2 of the revised Guidelines elaborates on the factors that an institution should consider in assessing materiality.

#### Removal of MAS notification requirement

The requirement to notify MAS before an institution commits to the commencement of or amends an existing material outsourcing arrangement has been removed from the revised Guidelines.

#### Requirements that apply to material outsourcing arrangements

Notwithstanding the removal of this expectation to pre-notify MAS, MAS will continue to assess and monitor the robustness of institutions' outsourcing risk management frameworks. Institutions are expected to exercise appropriate due diligence on their outsourcing arrangements and be able to demonstrate to MAS their observance of the Guidelines.

Following industry feedback, MAS has also provided for certain requirements to apply only to material outsourcing arrangements. These include the requirement:

- to perform periodic reviews on material outsourcing arrangements at least on an annual basis;
- to incorporate contractual clauses to allow the institution and MAS to be granted audit access and access to information and any report or finding made on the service provider and its sub-contractors; and
- to ensure that material outsourcing arrangements with service providers located outside Singapore are conducted in such a manner so as not to hinder MAS' supervisory efforts.

## Notification of adverse developments

Under the revised Guidelines, an institution is required to notify MAS as soon as possible of any adverse development arising from its outsourcing arrangements that could

impact the institution or the institution's group.

The description of "adverse developments" is now expressed to include any event that could potentially lead to prolonged service failure or disruption in the outsourcing arrangement, or any breach of security and confidentiality of the institution's customer information. This applies to both material and non-material outsourcing arrangements.

## Assessment of service providers

### Due diligence on service providers

The revised Guidelines require institutions to ensure that the service provider has been assessed to meet the regulatory standards expected of the institution, as if the outsourcing arrangement is performed by the institution.

Among other things, the due diligence should take into consideration the physical and IT security controls the service provider has in place, its business reputation and financial strength, and its ability to meet obligations under the outsourcing arrangement.

Information to be evaluated includes, *inter alia*, the service provider's risk management framework and capabilities (including technology risk management and business continuity management) in respect of the outsourcing arrangement.

### Due diligence on employees of service providers

Institutions are also expected to ensure that the employees of the service provider have been assessed to meet the institution's hiring policies

for the role they are performing, consistent with the criteria applicable to institutions' own employees. This is a new requirement under the revised Guidelines.

MAS has cited the following non-exhaustive examples of what should be considered under the employee assessment:

- whether they have been the subject of any proceedings of a disciplinary or criminal nature;
- whether they have been convicted of any offence (in particular, that associated with a finding of fraud, misrepresentation or dishonesty);
- whether they have accepted civil liability for fraud or misrepresentation; and
- whether they are financially sound.

## Outsourcing agreement

The revised Guidelines provide that each outsourcing agreement should have provisions that address, at minimum, the following aspects:

- scope of the outsourcing arrangement;
- performance, operational, internal control and risk management standards;
- confidentiality and security;
- business continuity management;
- monitoring and control;
- audit and inspection;
- notification of adverse developments;
- dispute resolution;
- default termination and early exit;
- sub-contracting; and
- applicable laws.

In relation to "*default termination and early exit*", the revised Guidelines also require that provisions should be put in place to ensure a smooth transition when the agreement is terminated or being amended. The agreement should be legally enforceable, including against a service provider that is an intra-group entity.

In relation to "*sub-contracting*", the revised Guidelines additionally require the institution to ensure that the sub-contracting of any part of a material outsourcing arrangement is subject to the institution's prior approval.

The contractual terms and conditions governing relationships, obligations, responsibilities, rights and expectations of contracting parties under the outsourcing agreement are required to be reviewed by a competent authority, such as the institution's legal counsel, for their legality and enforceability.

## Monitoring and control of outsourcing arrangements

Institutions are required to establish a structure for the management and control of their outsourcing arrangements.

In relation to material outsourcing arrangements, an institution is further required to:

- establish multi-disciplinary outsourcing management groups to ensure that all relevant technical issues and legal and regulatory requirements are met;

- establish outsourcing management control groups to monitor and control the outsourced service on an ongoing basis;
- conduct periodic reviews on all material outsourcing arrangements at least annually;
- prepare reports on the monitoring and control activities of the institution that are reviewed by senior management and provided to the board; and
- perform comprehensive pre- and post-implementation reviews of new or amended outsourcing arrangements.

## Audit frequency and scope

Under the revised Guidelines, an institution is required to ensure that independent audits and expert assessments of all its outsourcing arrangements, both material and non-material, are conducted.

In determining the frequency of an audit and expert assessment, the institution should consider the nature and extent of risk to and impact on the institution from the outsourcing arrangements.

The scope of the audits and expert assessments should include an assessment of the service providers' and its sub-contractors' security and control environment, incident management process (for material breaches, service disruptions or other material issues) and the institution's observance of the Guidelines in relation to the outsourcing arrangement.

## Outsourcing outside Singapore

Where the service provider engaged is, or the outsourced function is performed, in a foreign country, the revised Guidelines require an institution to take into account, as part of its due diligence, and on a continuous basis: (a) government policies; (b) political, social, and economic conditions; (c) legal and regulatory developments in the foreign country; and (d) the institution's ability to monitor effectively the service provider and execute its business continuity management plans and exit strategy.

The revised Guidelines further provide that the institution is expected to be aware of the disaster recovery arrangements and locations established by the service provider in this regard.

Where material outsourcing arrangements are entered into with service providers outside Singapore, these are required to be conducted in a manner so as not to hinder MAS' efforts to supervise the Singapore business activities of the institution in a timely manner.

## Outsourcing within a group

Similar to the previous Guidelines, the revised Guidelines apply to outsourcing arrangements with parties within the institution's group. MAS' expectations can be addressed within group-wide risk management policies and procedures.

The respective roles and responsibilities of each office in the outsourcing arrangement are required

to be documented in writing in a service level agreement or an equivalent document.

## Cloud computing

Notably, the revised Guidelines include a new section on cloud computing that sets out MAS' position on cloud computing.

An institution is expected to perform the necessary due diligence measures and apply the sound governance and risk management practices set out in the Guidelines when subscribing to cloud services.

The institution is required to adopt a risk-based approach to ensure that its level of oversight and control is commensurate with the materiality of risks posed by cloud services.

Among other things, an institution is required to:

- take active steps to address the risks associated with data access, confidentiality, integrity, sovereignty, recoverability, regulatory compliance and auditing;
- ensure that its service provider possesses the ability to clearly identify and segregate customer data using strong physical or logical controls; and
- have in place robust access controls to protect customer information that will survive the tenure of the contract of the cloud services.

## Application of Guidelines and self-assessment

The revised Guidelines apply from 27 July 2016 to all new outsourcing arrangements entered into by an institution.

Institutions are expected to conduct a self-assessment of all of their existing outsourcing arrangements against the Guidelines within three months from the issuance of the Guidelines (ie by 27 October 2016).

Institutions are required to rectify deficiencies identified in the self-assessments no later than 12 months from the issuance of the Guidelines (ie 27 July 2017).

## Contacts



**Lena Ng**  
Counsel

T: +65 6410 2215  
E: lena.ng  
@cliffordchance.com



**Sheena Teng**  
Senior Associate

T: +65 6506 2775  
E: sheena.teng  
@cliffordchance.com



**Esther Foo**  
Senior Associate

T: +65 6410 2203  
E: esther.foo  
@cliffordchance.com



**Zhern Leing Thai**  
Associate

T: +65 6410 2223  
E: zhernleing.thai  
@cliffordchance.com

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