BC FINANCIAL SERVICES AUTHORITY

Outsourcing Guideline

BC CREDIT UNIONS, INSURANCE AND TRUST COMPANIES

TABLE OF CONTENTS

INTRODUCTION

BCFSA Guidelines establish principles that regulated entities are expected to implement and follow as well as provide best practices on how to meet the objectives of the Guideline.

This Guideline sets out BCFSA's expectations for provincially regulated financial institutions incorporated in BC ("PRFIs") that outsource, or contemplate outsourcing, one or more of their business activities. These expectations are practices, procedures or standards that should be applied according to the characteristics of the outsourcing arrangement and the circumstances of the PRFI.

Financial institutions outsource business activities, functions and processes in order to meet the challenges of technological innovation, increased specialization and heightened competition as well as to improve efficiency and cost control. However, outsourcing can increase an institution's dependence on third parties, which may increase its risk profile. BCFSA, consistent with many financial sector regulators, is responding by introducing guidance related to the management of outsourcing risks.

PRFIs have the flexibility to configure their operations in the way most suited to achieving their corporate objectives. However, PRFIs retain ultimate accountability for all activities, regardless of whether they are outsourced or not. Therefore, BCFSA will regulate and supervise significant activities even if they are outsourced to a third-party provider.

PRFIs are expected to:

- ensure that the Board of Directors[1] is informed of outsourcing arrangements that are part of the business' significant activities;
- identify and evaluate the risks associated with existing and proposed outsourcing arrangements;
- develop a process for determining the materiality of arrangements;
- conduct due diligence, including evaluation of a service provider's reputation and ability to provide quality service and ensure data protection;
- ensure the Enterprise Risk Management framework ("ERM") includes the managing and monitoring of outsourcing risks; and
- document outsourcing arrangements with written contracts that address all relevant conditions that include regular review of the contracts for compliance and materiality (see the section on Outsourcing Contracts). The frequency of these reviews is to be determined by the PRFI; however, the reviews should be conducted at least once every three years.

[1] A reference to the Board of Directors can also include a Board committee, such as a Board committee established to examine specific issues.

SCOPE

This Guideline applies to all outsourcing arrangements of a PRFI. In applying this Guideline, the PRFI is expected to consider the impact of outsourcing arrangements on the PRFI and its consolidated operations. BCFSA's attention will be placed on outsourcing arrangements that are material or support significant activities of the PRFI.

All outsourcing arrangements should be subjected to the materiality assessment set out in the section on Management of Outsourcing Risk. BCFSA recognizes that outsourcing arrangements will exhibit varying degrees of materiality and expects that the robustness of a PRFI's management of outsourcing risks would be commensurate with the materiality of the arrangement.

PRFIs with outsourcing arrangements that are deemed material are expected to follow the full risk management expectations detailed in the Management of Outsourcing Risk section. The PRFI is expected to follow the expectations outlined in this Guideline for all outsourcing arrangements unless they are deemed clearly immaterial. The expectations apply to all organizations regardless of size. However, However, in undertaking its reviews, the supervisory intensity will depend on the nature, size, complexity, and risk profile of the PRFI, and the potential system impact of the PRFI's failure.

Definitions

For the purposes of this Guideline, the following definitions apply:

Outsourcing arrangement: an agreement between a PRFI and a service provider, whereby the service provider performs a business activity, function or process that is, or could be, undertaken by the PRFI. A PRFI may discuss with its BCFSA Relationship Manager when they are uncertain whether a particular arrangement falls within this definition. Examples are provided in Appendix 1.

Outsourcing contract*:* the document by which an outsourcing arrangement is codified in writing.

PRFI: a BC incorporated credit union, insurance company or trust company.

PRFI group: a group that includes a PRFI as well as any of the following: a) the entity that controls the PRFI if that entity is also a PRFI; b) a subsidiary of the PRFI; and c) a subsidiary of the entity referred to in a).

GOVERNANCE AND ACCOUNTABILITY

A PRFI retains ultimate accountability for all outsourced activities and is expected to support its monitoring, control and management of outsourcing risks through a sound governance structure.

BCFSA expects the roles and responsibilities for managing outsourcing risks to be defined, documented and incorporated in the PRFI's overall governance structure.

Board of Directors

The Board of Directors should:

- approve the policies that apply to outsourcing arrangements (e.g., outsourcing risk philosophy, materiality criteria, costs, ERM and approval limits);
- review a list of all the PRFI's material outsourcing arrangements and other relevant reports at least once per year; and
- ensure that a risk management program is applied.

The Board of Directors retains responsibility for the oversight(?) of the material outsourcing arrangements.

Senior Management

Senior management should:

- develop and implement the policies that apply to outsourcing arrangements (and any associated procedures) for approval by the Board of Directors as well as periodically review their effectiveness;
- review outsourcing contracts at least once every three years for compliance and materiality (see the section on Outsourcing Contracts);
- notify the Board of Directors of any issues with a service provider's compliance with the contract and develop action plans as needed;
- oversee maintenance of the centralized list of outsourcing arrangements;
- notify its BCFSA Relationship Manager immediately of any events that are likely to have a significant negative impact on compliance, operational error or the delivery of the service provided for by a material outsourcing arrangement;
- manage outsourcing costs; and
- ensure business continuity should the service provider(s) be unable to fulfill expectations.

Senior management will always retain overall accountability for an outsourcing arrangement.

Policies and Procedures

Policies and procedures should include:

1) An outsourcing risk philosophy reflected thein its ERM.

   The PRFI's outsourcing risk philosophy should comprise the PRFI's principles related to outsourcing, the basis for its decision making on outsourcing and the parameters for controlling outsourcing risks. Outsourcing risk philosophies will vary across PRFIs, but should address the following:

i. Integration of outsourcing arrangements, both individually and in aggregate, with overall business and strategic objectives. This could include an identification of any functions that, for strategic or internal control reasons, the PRFI would not contemplate outsourcing.

ii. Importance and adequacy of internal expertise and management frameworks to oversee and manage the outsourced activity and the relationship with the service provider.

iii. Short- and long-term cost implications, contingency plans and any relevant prudential and/or market conduct matters, such as concentration risk.

2) A materiality assessment for outsourcing arrangements. This assessment is expected to identify both the processes for determining the materiality of individual outsourcing arrangements and the underlying materiality factors such as those set out in the section on Materiality Assessments.

3) The expectations included in the section on Management of Outsourcing Risks integrated into the ERM and applied consistently throughout the PRFI. BCFSA expects management to pay particular attention to business continuity planning on an enterprise-wide basis (see the section on Business Continuity under Material Assessments).

4) Limits regarding the level or authority that enables the PRFI's officers to approve outsourcing arrangements of varying magnitudes, either individually or in aggregate. This system should be consistent with the outsourcing risk philosophy and materiality criteria.

ASSESSING THE MATERIALITY OF OUTSOURCING ARRANGEMENTS

A PRFI is expected to develop and implement a process for determining the materiality of outsourcing arrangements.

BCFSA recognizes that outsourcing arrangements may not be readily classified as either material or immaterial. In general, BCFSA expects that a PRFI will ensure that its ERM applies to all its outsourcing arrangements, except those that are clearly immaterial, and that the risk mitigants employed under this framework will be appropriate to the particular outsourcing arrangement. As such, the ERM should be scaled to apply different requirements depending on the type of outsourcing arrangement. Arrangements deemed material should be subject to the full expectations set out in the Management of Outsourcing Risk section unless it is reasonable to conclude that a particular expectation is not appropriate for the outsourcing arrangement in question. BCFSA may review a PRFI's materiality assessment on a case-by-case basis as part of the supervisory review process.

The materiality of an outsourcing arrangement will depend on the extent to which it has the potential to have an important influence—whether quantitative or qualitative—on a significant business line of the consolidated operations of the PRFI. Significant lines of business encompass not just those that are significant in size, but also those that are significant in decision making (e.g., treasury management).

The assessment of the materiality of an outsourcing arrangement is often subjective and depends on the circumstances faced by the PRFI. Without limiting the scope of the materiality assessment, factors that the FI should consider include:

1) The impact of the outsourcing arrangement on the finances, reputation and operations of the PRFI, or a significant business line, particularly if the service provider or group of affiliated service providers should fail to perform over a given period;
2) The ability of the PRFI to maintain appropriate internal controls and meet regulatory requirements, particularly if the service provider were to experience problems;
3) The cost of the outsourcing arrangement;
4) The degree of difficulty and time required to find an alternative service provider or to bring the business activity 'in-house';
5) The potential that multiple outsourcing arrangements provided by the same service provider can have an important influence – in aggregate – on the PRFI; and
6) The potential for privacy or confidentiality concerns.

Specific questions a PRFI might consider in assessing the materiality of outsourcing arrangements are set out in Appendix 2.

Outsourcing all or substantially all of a management oversight function[2] should always be considered material. For example, a material arrangement could relate to the outsourcing of a significant part of the PRFI's information technology function, investment management or loan processing.

Arrangements are less likely to be material where there are numerous similar providers in the marketplace and the costs and inconvenience of switching between providers are low. For example, if a PRFI outsources a function that several service providers can perform at a similar level of service, and it is easy to switch providers if necessary, then such an arrangement is less likely to be considered material.

[2] For the purpose of this Guideline, management oversight functions include a) financial analysis; b) compliance; c) any internal audit services related to the internal accounting controls, financial systems or financial statements; d) senior management; and e) risk management.

Significant changes in the volume or the nature of business conducted should cause the PRFI to reassess an outsourcing arrangement's materiality. In cases where an arrangement is reassessed as material, it should comply with this Guideline at the first opportunity, such as when the outsourcing contract is substantively amended, renewed or extended.

For its part, BCFSA will review the materiality of the outsourcing arrangements and may recommend that a PRFI consider an arrangement as being material. For example, BCFSA could recommend or suggest that an operational or systemic risk could arise where several PRFIs outsource to a single service provider. Should BCFSA make such a recommendation, the PRFI would also be informed of the risk of using a service provider that BCFSA has deemed inadequate.

Intra-group Outsourcing Arrangements

At a minimum, BCFSA expects the following to be addressed when an affiliated company enters into a material outsourcing arrangement with an entity that is a member of the same PRFI group:

- an outsourcing contract that details, among other things, the scope of the arrangement, the services to be supplied, the nature of the relationship between the PRFI and the service provider as well as procedures governing the subcontracting of services;
- an appropriate business continuity plan;
- a process for monitoring and oversight; and
- legislative requirements relating to location of records (refer to the section on Location of Records under Outsourcing Risk Management Framework).

As appropriate, a parent entity may address these expectations within enterprise-wide processes or plans as long as any specific risks to each subsidiary are addressed. As well, a parent PRFI may establish the program, approve the policies as well as develop and maintain the reporting on behalf of its PRFI subsidiaries.

Consistent with the risk-based Supervisory Framework, BCFSA may have additional expectations for PRFI group arrangements, depending on the risks related to the outsourcing arrangement and the conclusions of BCFSA's supervisory review.

Outsourcing Arrangements with the Auditor

A PRFI may obtain non-audit services from outsourced or "co-sourced" external or internal auditors. In such cases, a PRFI is expected to assure itself that the auditor is in compliance with the relevant auditor independence standards of the Canadian accounting profession, as well as any other applicable auditor independence requirements, for the services to be performed.

In addition, a PRFI should not outsource the following activities to its external auditor:

1) Any actuarial or treasury management service unless it is reasonable to conclude that the results of the service will not be subject to audit procedures during an audit of the PRFI's financial statements. For this purpose, actuarial services refer to the determination of an amount to be recorded in the financial statements of the PRFI or work normally undertaken by its appointed actuary. Actuarial services do not include services that involve assisting the PRFI in understanding the methods, models, assumptions and inputs used or advising management on the appropriate actuarial methods and assumptions that will be used. The PRFI may use an actuary working in the company's external auditor firm for the external review of the appointed actuary's work and reports.
2) Any internal audit service related to the internal accounting controls, financial systems or financial statements of the PRFI unless it is reasonable to conclude that the results of the service will not be subject to audit procedures during an audit of the PRFI's financial statements. This does not prohibit the external auditor from providing a non-recurring service to evaluate a discrete item or program, if the service is not, in substance, the outsourcing of an internal audit function.

OUTSOURCING RISK MANAGEMENT FRAMEWORK

A PRFI is expected to ensure its ERM appropriately manages and monitors risks commensurate with the materiality of the arrangements, paying particular attention to business continuity.

Risk Management Framework

In general, BCFSA expects that a PRFI’s ERM program applies to all outsourcing arrangements, except those that are clearly immaterial, and that the risk mitigants employed will be commensurate with the PRFI’s assessment of the risks associated with the particular outsourcing arrangement.

Business Continuity

A PRFI’s business continuity plan should address situations—either temporary or permanent—where the service provider fails to continue providing service. The business continuity plan and backup systems should be commensurate with the risk of a service disruption. In particular, the PRFI’s business continuity plan should ensure that the PRFI has in its possession, or can readily access, all records necessary to allow it to sustain business operations, meet its statutory obligations and provide all information as may be required by BCFSA in the event the service provider is unable to provide the service. The PRFI should also have an exit plan for when it is necessary to exit a material outsourcing arrangement.

Monitoring and Reporting

Every PRFI engaged in material outsourcing is expected to develop, implement and oversee procedures to monitor and control outsourcing risks in accordance with its outsourcing risk-management policies. The sophistication of the procedures should be commensurate with the size and complexity of the outsourcing arrangement(s) and with the expectations of this Guideline. Management is expected to prepare regular reports based on the PRFI's monitoring and oversight activities. These reports may outline the success of the outsourcing arrangement and the effectiveness of the ERM and may be reflected in the documentation delivered to the PRFI's senior management and the Board of Directors.

The PRFI is expected to maintain a centralized list of all its material outsourcing arrangements. A parent PRFI may maintain the list on behalf of the PRFI group. The list should contain information pertaining to the name of the service provider, the business function of the activity being outsourced, the date of the last review of the outsourcing arrangement and whether any sensitive information is involved. A template of a centralized list is provided in Appendix 3. The list should be updated on an ongoing basis and should form part of the documentation delivered to the PRFI's senior management. BCFSA may request access to the list at any time, at which point the PRFI is required to produce the records.

The PRFI is expected to monitor all material outsourcing arrangements to ensure that the service is being delivered in the manner expected and in accordance with the terms of the contract. Monitoring should include periodic reviews of the service provider, which would be commensurate with the level of risk involved and could include an assessment of the service provider's circumstances. These include the service provider's financial strength and technical competence as well as use and performance of significant subcontractors (e.g., obtaining the internal controls report and/or the SOC 2 audit report). Monitoring may also include regular formal meetings with the service provider.

The PRFI is expected to notify its BCFSA Relationship Manager within 14 days of any events that are likely to have a significant negative impact on the delivery of the service.

Location of Records

BCFSA expects PRFIs to maintain satisfactory facilities by which the Superintendent may obtain access to its records.[3] The PRFI should also ensure compliance with applicable Canadian laws and regulatory requirements, including the *Personal Information Protection and Electronic Document Act* and BC's *Personal Information Protection Act*. These requirements include records held by outsourcing service providers.

RISK ASSESSMENTS

A PRFI is expected to identify external and internal threats as well as potential failures in people, processes and systems on an ongoing basis. In addition, a PRFI is expected to promptly assess the vulnerabilities in material outsourcing arrangements and manage the resulting outsourcing risks in accordance with its risk tolerance.

[3] See section 133 of the *Financial Institutions Act.*

A PRFI is expected to assess its material outsourcing arrangements to ensure compliance with its risk tolerance, its outsourcing policies and procedures and the expectations of this Guideline. Assessments of material outsourcing arrangements should be periodically undertaken by the PRFI's internal audit department or another independent review function, either internal or external to the PRFI, provided it has the appropriate knowledge and skills and is commensurate with the resources of the PRFI.

PRFIs are expected to ensure that all relevant risks are identified and assessed. These include systemic risk arising from concentration in the provision of some outsourced and third-party services provided to PRFIs. Potential systemic risk could arise if, for instance, a sufficiently large number of PRFIs became dependent on one or a small number of service providers for the provision of critical services that were impossible or very difficult to substitute effectively and within an appropriate timeframe. Where there is no appropriate mitigant in place, a major disruption, outage or failure at one of these service providers could create not only a single point of failure with potential adverse consequences for the overall sector but could also have significant effects on the PRFI. For example, due to an event such as those listed above a service provider may need to prioritize its clients and a given PRFI may not be prioritized and therefore experience a significant disruption of the service being provided.

Assessments should test the PRFI's risk management activities for outsourcing to:

- ensure risk management policies and procedures for outsourcing are being followed;
- ensure effective management controls over outsourcing activities;
- verify the adequacy and accuracy of management information reports; and
- ensure that personnel involved in risk management for outsourcing are aware of the PRFI's risk management policies and have the expertise required to make effective decisions consistent with those policies.

Management should adjust the scope of the assessment depending on the nature of the outsourcing arrangement as well as the size and nature of the PRFI.

DUE DILIGENCE PROCESSES

A PRFI is expected to conduct due diligence, including evaluating the service provider's reputation and ability to provide quality service.

BCFSA expects a PRFI to conduct an internal due diligence to determine the nature and scope of the business activity to be outsourced (including any subcontracted outsourcing arrangements), its relationship to the rest of the PRFI's activities and how the activity is managed.

In selecting a service provider, or substantially amending or renewing an outsourcing arrangement, PRFIs are expected to undertake a due diligence process that fully assesses the risks associated with the outsourcing arrangement and addresses all relevant aspects of the service provider, including qualitative (i.e., operational) and quantitative (i.e., financial) factors. See Appendix 4 for a list of factors that could be included when performing due diligence of a service provider. PRFIs should also ensure they perform due diligence for any subcontracted outsourcing arrangements.

Due diligence processes will vary depending on the PRFI and on the nature of the outsourcing arrangement being contemplated. For example, in the case of renewals where no material change has occurred that would affect the viability of the outsourcing relationship, it may be appropriate to conduct more streamlined due diligence provided there are no other concerns, such as conflicts of interest.

OUTSOURCING CONTRACTS

A PRFI is expected to document outsourcing arrangements with written contracts that address all relevant conditions, including performance measures for the service provider to ensure it fulfills the contract conditions.

BCFSA expects material outsourcing arrangements to be documented by a written contract that addresses all elements of the arrangement and has been reviewed by the PRFI's legal counsel. For a list of suggested items to include in an outsourcing contract, please see Appendix 5. Some of the items identified in the appendix may not be applicable in all circumstances. However, PRFIs are expected to address all issues relevant to managing the risks associated with each outsourcing arrangement to the extent feasible and reasonable, given the circumstances and having regard to the interests of the PRFI.

INFORMATION SECURITY AND DISCLOSURE

BCFSA expects PRFIs to ensure that all outsourcing service providers comply with all applicable legislation, rules and BCFSA's *Information Security Guideline* in their treatment of information. The service provider is also expected to be able to logically isolate the PRFI's data, records and items in process from those of other clients at all times, including under adverse conditions.

PRFIs are expected to ensure that they provide appropriate disclosure to consumers if the PRFI shares consumers' information with an outsourcing service provider.[4] This includes providing the scope of information being shared, the service provider with whom it is being shared and the business function being outsourced.

[4] This is in accordance with the *Personal Information Protection Act* and the federal *Personal Information Protection and Electronic Document Act.*

APPENDIX 1: EXAMPLES OF OUTSOURCING ARRANGEMENTS

The outsourcing domain is diverse and growing. Some examples may include:

- information system management and maintenance (e.g., data entry and processing, data centres, facilities management, end-user support, local area networks, help desks);
- document processing (e.g., cheques, credit card slips, bill payments, bank statements, other corporate payments);
- application processing (e.g., insurance policies, loan originations, credit cards);
- policy administration (e.g., premium collection, policy assembly, invoicing, endorsements);
- claims administration (e.g., loss reporting, adjusting);
- loan administration (e.g., loan negotiations, loan processing, collateral management, collection of bad loans);
- investment management (e.g., portfolio management, cash management);
- marketing and research (e.g., product development, data warehousing and mining, advertising, media relations, call centres, telemarketing);
- back office management (e.g., electronic funds transfer, payroll processing, custody operations, quality control, purchasing);
- real estate administration (e.g., building maintenance, lease negotiation, property evaluation, rent collection);
- professional services related to the business activities of the PRFI (e.g., accounting, internal audit, actuarial);
- human resources (e.g., benefits administration, recruiting);
- complaint management;
- treasury management;
- sales distribution; and
- reinsurance.

This Guideline generally would not apply to the following:

- procurement of specialized training;
- discrete advisory services (e.g., legal opinions, certain investment advisory services that do not result directly in investment decisions, independent appraisals, trustees in bankruptcy);
- independent audit reviews;

- credit background and background investigation and information services;
- market information services (e.g., Bloomberg, Moody's);
- independent consulting;
- services the PRFI is not legally able to provide;
- repair and maintenance of fixed assets;
- supply and service of leased telecommunication equipment;
- correspondent banking services;
- maintenance and support of licensed software;
- temporary help and contract personnel;
- fleet leasing services;
- specialized recruitment;
- external conferences;
- clearing and settlement arrangements between members or participants of recognized clearing and settlement systems;
- sales of insurance policies by agents or brokers;
- ceded insurance and reinsurance; and
- syndication of loans.

APPENDIX 2: SAMPLE QUESTIONS TO ASSESS MATERIALITY

In assessing the materiality of a specific outsourcing arrangement, a PRFI may want to consider the following questions, among others:

- What is the relationship between the business activity and the PRFI's core business?
- What is the outsourcing arrangement's potential impact on earnings, solvency, liquidity, funding, capital, reputation, internal expertise, and capacity of the PRFI, brand value, or system of internal controls?
- What is the outsourcing arrangement's importance to achieving and implementing business objectives, the business strategy and business plans?
- What is the PRFI's aggregate exposure to a particular service provider? Is the PRFI exposed to additional outsourcing risk as a result of multiple outsourcing arrangements with a service provider?
- What is the size of contractual expenditures as a share of non-interest expenses of the PRFI or line of business?
- If the service provider is unable to perform the service over a given period:
    a. What is the expected impact on the PRFI's customers?
    b. What is the likely impact on the PRFI's reputation?
    c. Would it have a material impact on the PRFI's risk profile?
    d. Would the PRFI be able to engage an alternative service provider? How long would it take and what costs would be involved?

APPENDIX 3: EXAMPLE TEMPLATE FOR A CENTRALIZED LIST

Name of service provider	Short description of the arrangement	Type of arrangement (PRFI group, third party, etc.)	Country from which the service is provided	Start date of arrangement	Expiry or renewal date of arrangement	Estimated annual spending on the arrangement in the next year	Estimated value (dollar amount) of the arrangement	Date of last review	Business function	Sensitive information involved? (Y/N)

APPENDIX 4: DUE DILIGENCE OF SERVICE PROVIDERS

The due diligence of service providers may include, but is not necessarily limited to, examining a service provider considering these factors:

- experience and technical competence of the service provider to implement and support the outsourced activity. (This could include a review of the experience and technical competence of significant subcontractors where feasible);
- financial strength (e.g., most recent audited financial statements and other relevant information (to the best of the service provider's ability[5]);
- business reputation, complaints, compliance and pending litigation;
- internal controls, reporting and monitoring environment;
- the service provider's business resumption and contingency measures, including recovery testing, for ensuring the continuation of the outsourced business activity in the event of problems and events that may affect the service provider's operation (such as a systems breakdown, natural disaster, an inability of a significant subcontractor to provide services relevant to the outsourced activity and situations where extraordinary demands are placed on a service provider);
- reliance on and success in dealing with sub-contractors;
- potential conflicts of interest and data privacy concerns;
- insurance coverage; and
- business objectives, human resource policies, service philosophies, business culture and how they fit with those of the PRFI.

[5] BCFSA recognizes that the service provider is required to comply with other legislation (such as securities legislation) and might not be able to share certain information with the PRFI.

APPENDIX 5: ITEMS IN OUTSOURCING CONTRACTS

Outsourcing contracts should include, but is not necessarily limited to, the items outlined below.

Nature and Scope of the Service Being Provided

The contract is expected to specify the scope of the relationship, which may include provisions that address the frequency, content and format of the service being provided. The contract is expected to detail the physical location where the service provider will provide the service.

Performance Measures

Performance measures should be established to allow each party to determine whether the commitments contained in the contract are being fulfilled.

Reporting Requirements

The contract is expected to specify the type and frequency of information the PRFI receives from the service provider. This would include reports that allow the PRFI to assess whether the performance measures are being met and any other information required for the PRFI's monitoring framework (see the section on Management of Outsourcing Risk). In addition, the contract is expected to include procedures and requirements for the service provider to report events to the PRFI that may have the potential to materially affect the delivery of the service.

Resolution of Differences

The contract is expected to incorporate a protocol for resolving disputes. The contract should specify whether the service provider must continue providing the service during a dispute and the resolution period as well as the jurisdiction and rules under which the dispute will be settled.

Defaults and Termination

The contract is expected to specify what constitutes a default, identify remedies and allow for opportunities to cure defaults or terminate the arrangement. The PRFI is expected to ensure that it can reasonably continue to process information and sustain operations if the outsourcing arrangement is terminated or the service provider is unable to supply the service. Appropriate notice should be required for termination of service and the PRFI's assets should be returned in a timely fashion. Data and records relating to data processing outsourcing arrangements should be returned to the PRFI in a format that would allow the PRFI to sustain business operations without prohibitive expense.

The contract should not contain wording that precludes the service from being continued in situations where the Superintendent takes control of the PRFI or where the PRFI is in liquidation.

Ownership and Access

Identification and ownership of all assets (intellectual and physical) related to the outsourcing arrangement should be clearly established, including assets generated or purchased pursuant to the outsourcing arrangement. The contract should state whether and how the service provider has the right to use the PRFI's assets (e.g., data, hardware and software, system documentation, or intellectual property) and the PRFI's right to access those assets.

Contingency Planning

The contract should outline the service provider's measures for ensuring the continuation of the outsourced business activity in the event of problems and events that may affect the service provider's operation, including systems breakdown, natural disaster and other reasonably foreseeable events. The PRFI should ensure that the service provider regularly tests its business recovery system as it pertains to the outsourced activity, notifies the PRFI of the test results and addresses any material deficiencies. In addition, the PRFI should be notified if the service provider makes significant changes to its business resumption and contingency plans or encounters other circumstances that might have a serious impact on the service. PRFIs should also ensure that the service provider has the capacity to provide timely service even in the event of multiple demands on its services (e.g., for reinsurance, if there are multiple natural disasters affecting the reinsurer's clients). BCFSA may request the service provider's contingency planning test results at any time.

Audit Rights

The contract is expected to clearly stipulate the audit requirements and rights of both the service provider and the PRFI. At a minimum, it should give the PRFI the right to evaluate the service provided, or alternatively to have an independent auditor evaluate it on its behalf. This includes a review of the service provider's internal control environment as it relates to the service being provided.

In addition, in all situations—irrespective of whether an activity is conducted in-house, outsourced, or otherwise obtained from a third party—BCFSA retains its supervisory powers. Accordingly, an undertaking from the service provider or a provision in the outsourcing contract should give the BCFSA or the Superintendent's representative the right to:

- exercise the contractual rights of the PRFI relating to the audit;
- accompany the PRFI (or its independent auditor) when it exercises its contractual audit rights;
- access and make copies of any internal audit reports (as well as associated working papers and recommendations) prepared by or for the service provider in respect of the service being performed for the PRFI, subject to BCFSA agreeing to sign appropriate confidentiality documentation in form and content satisfactory to the service provider; and

- access findings in the external audit of the service provider (as well as associated working papers and recommendations) that address the service being performed for the PRFI, subject to the consent of the service provider's external auditor and BCFSA agreeing to sign appropriate confidentiality documentation in form and content satisfactory to the service provider and the external auditor.

BCFSA will provide the PRFI with reasonable notice of its intent to exercise its audit rights and share its findings with the PRFI where appropriate. In the normal course, BCFSA would seek to obtain information it requires through the PRFI itself.

Subcontracting

The contract is expected to set out any rules or limitations to subcontracting by the service provider. Security and confidentiality standards should apply to subcontracting or outsourcing arrangements by the primary service provider.

Consistent with the principles of this Guideline, the audit and inspection rights of the PRFI and BCFSA should continue to apply to all significant subcontracting arrangements.

Pricing

The contract should fully describe the basis for calculating fees and compensation relating to the service being provided.

Insurance

The service provider should be required to notify the PRFI of significant changes in insurance coverage and disclose general terms and conditions of the insurance coverage. The PRFI may also wish to require a minimum level of insurance coverage and outline the liability of the service provider and the PRFI.

Confidentiality, Security and Separation of Property

At a minimum, the contract is expected to set out the PRFI's requirements for confidentiality and security. The PRFI should ensure that it remains in compliance with applicable privacy laws (for example, the *Freedom of Information and Protection of Privacy Act* and the federal *Privacy Act*) and laws governing the location of records.

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