



Westpac New Zealand Limited

Submission to the Reserve Bank of New
Zealand on the Consultation Paper:
*Review of the outsourcing policy for
registered banks*
4 December 2015

Mark Weenink
General Manager, Regulatory Affairs
Compliance and General Counsel NZ
Westpac New Zealand Limited

Loretta DeSourdy
Head of Regulatory Affairs
Westpac New Zealand Limited

1. INTRODUCTION

1.1 This submission to the Reserve Bank of New Zealand (**Reserve Bank**) is made on behalf of Westpac New Zealand Limited (**WNZL**) in respect of the Consultation Paper: *Review of outsourcing policy for registered banks (Consultation Paper)*. We appreciate the opportunity to provide feedback on the Reserve Bank's proposals and the extension of time the Reserve Bank provided for submissions. We are keen to engage further with the Reserve Bank on the development of the policy and would welcome the opportunity to discuss our submissions with you.

1.2 WNZL wishes to retain confidentiality of this information and requests that the Reserve Bank contact WNZL before its release.

1.3 WNZL's contact for this submission is:

Loretta DeSourdy
Head of Regulatory Affairs
Westpac New Zealand Limited
PO Box 691
Wellington



1.4 The review of the Reserve Bank's Outsourcing Policy (**BS11**) is timely given the current policy was released in 2006 and the Reserve Bank's recent outsourcing stocktake exercise revealed that banks had adopted different interpretations of BS11. The review provides the Reserve Bank with the opportunity to assess the appropriateness of the current policy and clarify its expectations about outsourcing, which ultimately will assist both registered banks and the regulator.

1.5 The Consultation Paper has left some key issues, such as what constitutes basic banking services, to be decided following the Reserve Bank's consideration of the submissions. We understand that this has been done so that the Reserve Bank can obtain feedback on these matters to assist with its determination. This is helpful but WNZL recommends that the Reserve Bank undertake further consultation before the policy is finalised so that submissions can be sought on this important additional detail. A workshop with the industry would also be useful at that stage.

1.6 As requested, WNZL has responded to the Reserve Bank's questions using the template provided but also makes its key submissions below and sets out a possible framework for the policy in Section 3 of this submission.

2. KEY SUBMISSIONS

Balancing Risks

2.1 WNZL does not agree that there has been evidence of a market failure in banks' management of outsourcing risk which supports the Reserve Bank using its powers under s68 of the Reserve Bank of New Zealand Act (**RBNZ Act**) to impose

requirements along the lines of those proposed. On this basis we believe that a large number of the proposals in the Consultation Paper are not warranted.

- 2.2 The policy proposals do not appear to have taken into account the concept of materiality, despite the high materiality thresholds that are contemplated in paragraph 25 of the Consultation Paper, which refers to "*material disruption*" and paragraph 26, which refers to the potential damage being "*sufficiently serious to threaten the bank's survival to the extent that the soundness of the system was at risk*" or the failure being "*sufficiently damaging to satisfy us that the "significant damage" threshold in s68(b) would be relevant*".
- 2.3 In addition, the policy proposals do not appear to balance the risks identified in paragraph 24, which are considered to be very low probability, with the significant benefits that banks derive from outsourcing. These benefits are acknowledged by the Reserve Bank in the Consultation Paper and are referred to in more detail in our responses to Questions 1 and 9. Outsourcing provides New Zealand banks with access to a much broader and specialised pool of talent, technology and infrastructure and allows them to draw on international capability that may not otherwise be available to them.
- 2.4 An assessment of the likely implementation costs also reveals a material imbalance with the risks identified in paragraph 24. The scope of the proposals is uncertain because some matters, such as what constitutes basic banking services are still to be determined, so the cost cannot be estimated with any degree of accuracy. However, a high level initial estimate of the implementation cost to the industry could be [REDACTED] WNZL's initial estimate is that its implementation cost could [REDACTED] with an additional [REDACTED] in operating costs. [REDACTED]
- 2.5 Further consideration should be given to the small scale of the New Zealand market and hence the public good and commercial benefits of outsourcing. This is relevant not only for the cost of scale benefits, but also so that New Zealand's registered banks can obtain the required depth of skills and knowledge that outsourcing can provide and which may not otherwise be available. In a small market more weight should be applied to the commercial benefits of outsourcing.
- 2.6 Rather than imposing restrictive conditions on outsourcing, with the resultant considerable compliance and operational costs to deal with low probability events, WNZL recommends that further work be done on a trans-Tasman legislative solution. The 2006 amendments to the New Zealand and Australian legislation to incorporate the recommendations of the Trans-Tasman Council on Banking Supervision, noted by the Reserve Bank as a "*path-breaking advance in home-host supervisory cooperation*" do not appear to have had any impact on regulatory policy making. The legislation should be revisited with a view to strengthening those provisions.

Linking of the Policy Intent to the Operational Outcomes

2.7 The Consultation Paper does not contain a clear description of what policy outcome the Reserve Bank is seeking. There are three key matters which require clarification:

- (a) What failure event(s) does the policy seek to address – a bank failure/resolution or separation, or also third party supplier failure, or prolonged business as usual outage? While paragraph 49 sets out functions that a failed bank would need in order to support Open Bank Resolution (**OBR**), the focus elsewhere is on the failure of a related party service provider rather than other providers.
- (b) What core functions are in scope? Currently there is some conflict between paragraph 49, which lists the outcomes a bank would need to be able to continue to undertake in a failure event, and paragraph 55, which states what must be included in the separation plan. In other places, such as the notification and compendium requirements, all outsourcing arrangements are in scope. WNZL proposes that the policy only apply to outsourcing that is relevant to a core function and only where it is material. This proposed approach is set out in more detail in Section 3 where the concepts of core function and basic banking services are discussed.
- (c) What operational outcomes is the Reserve Bank seeking? The outcomes listed in paragraph 49 do not link to a concept similar to “legal and practical control” or to timeframes in which they must be delivered. These would seem to be required in order for the policy to be effective. The concept of Required Operational Outcomes is also included in our suggested framework.

2.8 WNZL supports the Reserve Bank’s proposal to retain an outcomes-focused approach to the outsourcing policy. An outcomes focus provides banks with flexibility to arrange their affairs in a manner that best suits their operational and business model while at the same time achieving the Reserve Bank’s policy objectives. The required operational outcomes within the policy will need to be clear so they are not capable of being misinterpreted. However, the level of prescription currently proposed is not entirely consistent with an outcomes focus.

[REDACTED]

■

[REDACTED]

■

[REDACTED]



Prohibition on Outsourcing to Related Parties

- 2.11 The policy objectives can be accomplished without imposing a blanket prohibition on outsourcing specific functions to a related party. The focus should be on the required policy outcomes being met and not on the operational means of achieving the outcomes. Banks should be permitted to achieve the outsourcing policy objectives in the optimal manner to them. Outsourcing to related parties should be permitted where robust contingent arrangements are in place. These arrangements would need to enable the New Zealand bank to function independently in the event that the outsourced function is no longer available. They would need to reliably deliver the required operational functionality within the required timeframes and be both testable and sustainable.
- 2.12 The prohibition on outsourcing certain activities runs counter to internationally accepted practice where key systems are managed via centralised models to minimise the risk of non-integrated system deviation and to meet market expectations for global capability. For example, most global banking risk models rely on a centralised capability which maintains model methodology and critical system oversight and maintenance. The system is then leased out to the regions in which the bank operates.

Compendium and Engagement

- 2.13 WNZL agrees that a tool facilitating visibility of a bank's outsourced functions is sensible but does not consider that this tool needs to be a separate compendium requirement. A requirement that a bank must be able to generate a report containing the relevant details of the outsourced functions should be sufficient. This would minimise inefficiency by permitting a bank to choose an appropriate (and likely pre-existing) tool, to achieve the same outcome as the compendium. A separate compendium requirement could, depending on the drafting of the requirement, create a risk that an omission from the compendium could result in the bank being non-compliant with its outsourcing conditions of registration. The recent Regulatory Stocktake Consultation Document proposed that the drafting of conditions of registration minimise the scope for any genuinely trivial matters to result in breaches of binding requirements. WNZL considers that this is a case where this should apply so that a bank would not be non-compliant with its conditions of registration for an omission from the compendium.
- 2.14 WNZL considers that banks should remain responsible for assessing whether their outsourcing arrangements comply with the policy and could provide the Reserve Bank with their BS11 compliance assessments if requested. However, if notification is regarded as necessary, option two in the Consultation Paper is preferred but should be restricted to arrangements that relate to a core function and only where they are material. This concept is discussed further in the framework set out in Section 3. The reporting tool and BS11 assessment along with further clarification of the policy requirements and outcomes should make the engagement approach proposed in the Consultation Paper unnecessary.

Outsourcing Policy Threshold

- 2.15 The threshold at which the outsourcing policy applies should be retained at the existing level of \$10 billion of external liabilities. A threshold of \$1 billion will capture small banks whose failure would not create an impact on the soundness of the New Zealand financial system and therefore the regulatory intervention proposed would not appear to be justified. The application of the outsourcing policy to these smaller entities is also inconsistent with the statements in paragraphs 25 and 26 of the Consultation Paper, noted above in paragraph 2.2. It could also represent a barrier to entry or could cause some banks to leave the New Zealand market due to the initial and operational compliance costs.

Timelines

- 2.16 Finally, the timelines proposed to agree a compliance plan with the Reserve Bank and to implement that plan are ambitious (based on the Reserve Bank's proposed policy). WNZL estimates that the time needed to complete a plan is from [REDACTED] as the plan would need to involve considerable input from WNZL and WBC business, regulatory and technology teams and would need to be approved by both Boards. [REDACTED]

[REDACTED] There would also be a compound effect on timeframes due to sequencing requirements and the need to have restrictions on multiple system deployment in order to avoid increasing operational risk.

3. PROPOSED POLICY FRAMEWORK

- 3.1 As an embodiment of a number of WNZL's submissions herein, in this section we propose a possible policy framework in relation to key policy matters, together with associated definitions. WNZL considers that this captures the Reserve Bank's policy objectives, whilst assisting in creating clarity and consistency as to the scope and application of the proposed policy.
- 3.2 The outsourcing policy needs to identify the **Key Policy Requirements**, which should have a consistent scope of outsourcing associated with them (**Scope of Outsourcing**) as set out below. WNZL recommends that these Key Policy Requirements are:
- (a) Required Operational Outcomes in a Failure Event;
 - (b) Outsourcing Arrangements Repository;
 - (c) Reserve Bank Engagement Process; and
 - (d) Governance and Operational Frameworks.

These concepts are set out in more detail below.

Scope of Outsourcing

- 3.3 WNZL recommends that the Scope of Outsourcing in relation to any function, applicable to each of the Key Policy Requirements require that:
- (a) the function is Outsourced (as defined in paragraph 3.4 below);
 - (b) the function is relevant to a Core Function; and
 - (c) the function is material (as defined below at paragraph 3.8) to the provision of that Core Function.
- 3.4 WNZL proposes the following as an alternative to the definition of Outsourcing set out in the Consultation Paper:
- Outsourcing is defined in this policy as the use of a third party (either an affiliated entity within a corporate group or an entity that is external to the corporate group) to perform tailored business processes on a continuing basis that would normally or routinely be undertaken by a registered bank.*
- 3.5 The use of the term "*tailored business processes*" is intended to exclude the procurement or sourcing of generic goods and services. The use of the word "*would*" rather than "*could*" together with the use of the term "*normally or routinely*" is regarded as more appropriate as "*could*" is unlimited in its application. "*Would*" still allows for future proofing as the relevant arrangements will be considered at the point in time when the outsourcing occurs and therefore will capture a bank's evolving products and services.
- 3.6 If an activity meets the definition of Outsourcing, it must then be determined whether it is relevant to a Core Function.
- 3.7 It is proposed that the Core Functions be defined as follows, drawing on the Reserve Bank's policy objectives identified in paragraphs 49 and 55 of the Consultation Paper:
- (a) Meeting the bank's daily clearing/interchange and counterparty settlement obligations¹;
 - (b) Understanding the bank's credit, market and liquidity risk positions;
 - (c) Having access to relevant systems and balance sheet data which enables the bank to calculate its financial position and undertake its prudential regulatory reporting;

¹ Note that the reference to "*other time-critical obligations*" has not been included as it does not appear to add anything.

- (d) The provision of Basic Banking Services (as defined below) to existing customers. Consistent with the OBR Policy, we propose that Basic Banking Services includes:
 - (i) consumer and small business customers having access to their transaction accounts, that is, being able to make deposits and withdrawals, to service their existing loans and other basic credit facilities, to apply for new credit, and to provide account activity reporting;
 - (ii) in terms of channels, access only to branches, ATMs, and online banking; and
 - (iii) in terms of payment instruments and methods, access to cash, debit cards, credit cards, and direct credits.

3.8 If an activity is relevant to a Core Function, separate consideration must then be given to whether the arrangement is material. A contract or arrangement would be material if:

- (a) the functions that would be disrupted or the costs that would be incurred if the service could not be delivered would threaten the bank's survival to the extent that the soundness of the financial system was at risk;
- (b) the product or service is not readily substitutable by customers; and
- (c) it is critical to the delivery of the relevant Core Function.

Required Operational Outcomes in a Failure Event

3.9 The concept of required operational outcomes, together with the circumstances in which they must be able to occur, should be made clearer and more consistent in the proposed policy. WNZL recommends that this be embodied in the concepts of **Required Operational Outcomes** and **Failure Events** as defined below.

3.10 **Required Operational Outcomes** is proposed to be defined as "*the ability to have legal and practical control over functions that are within the Scope of Outsourcing in the event that a Failure Event occurs, within the specified timeframes (as set out in the current Outsourcing Policy)*".

3.11 A **Failure Event** is defined as:

- (a) the bank fails;
- (b) the bank separates from its parent;
- (c) a third party service provider of an outsourced function within the Scope of Outsourcing fails; or
- (d) there is a prolonged business as usual outage of a function within the Scope of Outsourcing, and the outage disruption is sufficiently serious as to threaten

the bank's survival to the extent that the soundness of the New Zealand financial system is at risk.

- 3.12 The proposed policy framework has no prohibition on particular activities being outsourced and there is no concept of required contractual provisions in Outsourcing contracts. Instead there is an **outcomes based focus** on the Required Operational Outcomes.
- 3.13 Where a contingency arrangement is used as one form of practical control, then it must be:
- (a) reliably deployable within the required timeframes;
 - (b) testable; and
 - (c) sustainable.

Outsourcing Arrangements Repository

- 3.14 The policy should provide that a bank must be able to generate a report of its outsourcing contracts, rather than a separate compendium requirement. The report would need to contain relevant details pertaining to the arrangements consistent with Appendix two of the Consultation Paper. This would allow banks to use their existing contract management databases. Outsourcing arrangements that meet the policy definition of outsourcing could be flagged so that a report could be generated at any time. Requisite information including contract description, start and expiry dates, supplier name, business unit owner and supply classification could be accessed and printed on request.

Reserve Bank Engagement Process

- 3.15 The policy should not require that banks engage with the Reserve Bank over individual outsourcing arrangements. Banks should be able to undertake the requisite risk assessment and due diligence of their arrangements (on the basis of the governance and operational frameworks) to ensure they meet the requirements of the outsourcing policy, as occurs with other condition of registration compliance. Banks should be able to seek the Reserve Bank's advice where the assessment process raises any uncertainty or where they need some assurance before investing in a significant outsourcing arrangement. In those situations, the expectation is that the Reserve Bank would provide written reasons for its decision, which a bank could rely on.
- 3.16 The Reserve Bank will be able to monitor banks' compliance by requesting the BS11 assessment for any in scope outsourcing arrangement (i.e. a bank's internal assessment of how it is meeting the Required Operational Outcomes). This monitoring will also allow the Reserve Bank to assess whether banks are adopting a consistent approach to the interpretation of the policy.

Governance and Operational Framework

- 3.17 The policy should require banks to have proper governance and operational frameworks in place to ensure that outsourcing risk addresses the Reserve Bank's outsourcing policy.
- 3.18 Requirements should include:
- (a) an outsourcing risk appetite statement approved by the Board;
 - (b) an outsourcing policy;
 - (c) a supplier governance framework;
 - (d) a separation plan;
 - (e) a BS11 compliance plan capturing legal and practical controls for all outsourcing arrangements within the Scope of Outsourcing; and
 - (f) a BS11 assessment capturing details of how the arrangement meets the Required Operational Outcomes for all outsourcing arrangements within the Scope of Outsourcing.

RESPONSES TO CONSULTATION QUESTIONS

Q1	<p>Do you agree with the analysis of the problem? Do you agree that the issues identified in paragraph 24 appropriately identify the potential problems with the banks' use of outsourcing?</p> <ul style="list-style-type: none">▪ WNZL does not agree that there has been evidence of a market failure in banks' management of outsourcing risk and considers that to the extent there is a problem that needs to be addressed, consideration should be given to enhancing the trans-Tasman legislation that was put in place in 2006. In practice the identified risks have a very low likelihood of occurring and in fact may not be any more apparent as a result of outsourcing, such that the adverse efficiency impacts of the proposed policy are likely to significantly outweigh the identified benefits. Outsourcing provides cost efficiencies and capability improvements that have direct benefits to customers and shareholders, and consequently to the financial system and it is important that these benefits are balanced with the perceived risks.▪ Banks are very conscious of the robustness of any outsourcing capability where it could disrupt the provision of services, given the potential impacts on their customers and profits. These provide very real incentives to ensure the arrangements are robust. The arguments set out in paragraphs 19 and 20 that there is potential market failure are considered to be fairly weak and are the Reserve Bank's only stated justification for intervening.▪ The Consultation Paper notes in paragraph 24(a) that outsourcing may increase the risk of a bank (or banks) failing. While there is agreement that a bank failure can cause significant damage to the financial system, it is not as clear that failure of a bank's outsourcing arrangements would. In practice, there appears to be few instances where a bank has failed because of the failure of a service provider. The Consultation Paper refers to a material disruption to services because of supplier failure or where the service provider has made an error. While both are possible, there is no evidence that outsourcing itself leads to a higher risk of these scenarios occurring.▪ Outsourcing may in fact reduce operational risk. The robustness of a function may be improved by it being performed by specialist expert entities that are incentivised to perform to a high standard in order to continue to be engaged and to ensure contractual penalties are avoided. While the bank may be exposed to a failure of a third party, it is reducing the risk of failure of internal capabilities. Further, there would need to be multiple contemporaneous outsourcing failures to create a plausible increase in the risk of a bank failure.▪ Outsourcing also provides access to a much broader and specialised pool of talent, technology and infrastructure and allows banks to draw on international capability that may not otherwise be available to them. A third party provider's resource, infrastructure capability, and customer base means it may be better able to manage volume spikes and demand for services. Risks associated with supplier failure are mitigated by having business continuity plans (BCPs) in place with suppliers which are tested on a regular basis for interruptions to service.▪ The Consultation Paper states that outsourcing may increase the risk that there will be problems resolving a bank if it fails. While it is feasible that outsourcing might hamper bank resolution in some cases, the converse is also likely to apply. Being
----	--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------

able to rely on outsourced suppliers to continue providing critical services in a bank failure event might actually mitigate the risk. Provided the third party continues to be paid, it will continue to deploy its staff to run or support services and software without interruption as failure to do so would be sub-optimal from both a commercial and legal perspective.

- The balance of probability is that outsource arrangements will:
 - spread the risk of bank system and process failures (because activities are not concentrated at the bank); and
 - simplify the business that needs to be managed in-house by the statutory manager in the event of a bank failure.
- It is also more efficient and cost effective to switch out an outsource partner if there is a problem with them than it is to invest in trying to fix in-house systems and processes and secure the specialist technical expertise. It is acknowledged that these arguments do not hold as well in respect of the outsourcing of multiple functions to one party but this risk could be dealt with through the concept of materiality that WNZL is recommending be applied to the policy.
- In terms of outsourcing to a parent bank or other related party, the Consultation Paper does not explain why the parent bank would be unwilling to continue to provide services to the New Zealand bank post separation or why it would be unable to do so. It is not evident why the Australian regulator would choose to discontinue the provision of services to the New Zealand subsidiary in this situation. It would seem counter-productive to immediately discontinue services to the New Zealand banking operation when a significant number of Australian and global bank customers would have trans-Tasman or Asia-Pacific operations necessitating the continuation of New Zealand banking relationships and arrangements. However, the risk that the overseas regulator may do so is what appears to drive the proposed policy changes. The expectation is that Australian and New Zealand regulators would work closely together to manage a failure. It seems unlikely that the parent bank would not continue to operate in a failure situation given the systemic importance of the Australian banks to that economy.
- Requiring New Zealand banks with overseas parent banks to spend considerable sums of money to replicate global systems, applications, and people capability for the sole purpose of pre-positioning against the low risk of a parent bank failure is a disproportionate response and will lead to significant costs, risks and inefficiencies. The Reserve Bank acknowledges in paragraph 12 that there is a trade-off in section 68 of the RBNZ Act between soundness and efficiency but it is questionable whether the proposals strike the right balance in this trade-off.
- The Reserve Bank is proposing restrictions on outsourcing to a related party at the same time as Australia is proposing that Australian banks be subject to increased capital requirements, which should make the prospect of a major Australian bank failing less likely. The Financial System Inquiry (**FSI**) in Australia has recommended that the capital levels for Authorised Deposit-Taking Institutions (**ADIs**) be raised "*to ensure they are unquestionably strong*". The FSI recommended as a baseline target for capital ratios that Australian ADIs be in the top quartile of internationally active banks. In its response to the FSI report, the Australian Government agreed with the unquestionably strong recommendation and supported and endorsed the Australian Prudential Regulatory Authority (**APRA**) to implement this recommendation. These

	<p>new capital requirements should give the Reserve Bank additional comfort that New Zealand banks with Australian ADI parents are part of a robust and financially sound banking group.</p> <ul style="list-style-type: none"> ▪ The Reserve Bank has observed that outsourcing may create issues that may undermine the maintenance of a sound and efficient financial system. The example given is a prolonged disruption to the payments system caused by a technology failure. It is agreed that a prolonged payments outage could be disruptive to customers and might impact the wider financial system if it was ongoing but these impacts would be possible whether or not the disrupted system was outsourced. There is no evidence that outsourcing a system, or outsourcing the support for an in-house system, increases the risk of system disruption. As mentioned above, it may actually decrease this risk because the bank is using specialist service providers and spreading the bank's capability and operational risk. ▪ The Consultation Paper notes that another reason for regulatory intervention in the outsourcing area is because there may be issues around concentration risk associated with a single supplier to many banks. However, the Consultation Paper does not provide any detail on how the Reserve Bank's policy proposals would deal with this issue. Banks should be responsible for ensuring that their outsourcing arrangements are robust and contain provisions appropriate for those arrangements. The fact that there may only be one or two suppliers in the market for a particular service should not be sufficient reason to prohibit the outsourcing provided all relevant risk factors have been duly considered and weighed by the bank. Where the outsourced supplier provides services to more than one New Zealand bank, the focus should be on appropriate risk mitigants, such as robust vendor disaster recovery (DR) and BCP arrangements and possibly pan-bank contingency deeds entered into between the affected banks. It would not be appropriate to direct banks to have alternative supplier contingency arrangements when there are none available, and it would be neither commercially viable nor operationally realistic to expect banks to rebuild in-house capability and infrastructure to insource these services – particularly considering in most instances, technology, infrastructure and people capability will have moved on significantly since the service was outsourced. However, where there is only one service provider in the market a bank would assess the risk to determine if it was acceptable and could explore options to encourage alternative vendors in the market.
<p>Q2</p>	<p>Without an outsourcing policy how would you propose that a failure is managed?</p> <ul style="list-style-type: none"> ▪ While many of the policy objectives would be met by a bank having robust internal policies and processes to deal with supplier governance and operational risk, BCPs, and a separation plan for parent bank dependencies, having an outsourcing policy in the prudential framework helps ensure that a bank is able to negotiate the necessary provisions with third-party suppliers. This is because it provides a regulatory rationale for the controls and requirements which many suppliers would not otherwise provide. ▪ WNZL considers that the policy should place more reliance on self-discipline rather than on regulatory discipline as currently proposed. As currently drafted, the proposals would require that banks engage with the Reserve Bank for: <ul style="list-style-type: none"> ○ all outsourcing arrangements; ○ the outsourcing compendium; and

	<ul style="list-style-type: none"> ○ the separation plan. ▪ This will significantly increase the compliance burden on the affected banks. It is also at odds with the approach taken by other prudential regulators whose approaches provide banks with more flexibility to configure their operations in the manner most suited to their objectives while still being accountable for those arrangements. ▪ If the detailed requirements regarding notification, the compendium and the separation plan are set out in conditions of registration, the risk of a bank being non-compliant with the outsourcing condition of registration could significantly increase. The conditions do not normally allow for a concept of materiality with respect to non-compliance. Consequently, depending on the drafting of the conditions, a bank could be compliant with all other aspects of the outsourcing policy but be non-compliant because it failed to identify an arrangement as one which must be notified to the Reserve Bank and included in its compendium. ▪ The Reserve Bank's proposal that all outsourcing arrangements (regardless of how immaterial) will need to be notified so that a determination can be made as to whether a non-objection notice will be required, is a major shift from the current policy and prudential regulatory regime which allows banks to manage their affairs. ▪ WNZL considers that the outsourcing policy should provide high level guidelines for the oversight and supervision of genuine outsourcing risk in relation to material arrangements impacting core functions, and not be focused on operational and business risk arising from general procurement and non-material outsourcing arrangements.
Q3	<p>Do you agree that the current outcomes-focus should be retained?</p> <ul style="list-style-type: none"> ▪ Yes, WNZL supports retaining an outcomes-focused approach to the outsourcing policy. While the Reserve Bank says an outcomes approach remains broadly appropriate the level of prescription proposed in the Consultation Paper appears to be at odds with this statement. ▪ An outcomes focus should provide banks with more flexibility to arrange their affairs in a manner that best suits their operational and business model while at the same time achieving the Reserve Bank's policy objectives. Clarity of the outcomes and how they are to be met in a practical banking context would avoid the range of interpretations that banks appear to have taken with the current policy. ▪ As mentioned above, the outsourcing policy should be concerned with material outsourcing of core functions rather than all outsourcing arrangements, including what would more usually be considered general procurement. The proposed policy makes no reference to materiality and apart from the list of matters not considered to be outsourcing appears to contemplate that all outsourcing arrangements should be treated in the same manner. That is, all outsourcing arrangements will need to be notified to the Reserve Bank and included in the compendium. However, each bank will have a significant number of low risk outsourcing arrangements that will not have an impact on financial stability if a service provider failed. ▪ In our discussion with Reserve Bank staff it was confirmed that the reference to regulatory reporting in paragraph 70 was intended to refer to Reserve Bank reporting. The assumption is that the reference in paragraph 42 to "<i>the ability of the bank to meet regulatory and legal obligations</i>" is therefore similarly limited to prudential obligations and not any broader regulatory or legal obligations which may be covered

	by other regulators' requirements.
Q4	<p>Do you agree that changing the objectives to focus more on resolution is right?</p> <ul style="list-style-type: none"> ▪ A resolution focus provides additional comfort to the regulator that the bank retains a focus on continuing operations post failure. However, all four Failure Events remain relevant to an outsourcing policy.
Q5	<p>Do you agree that the current outcomes are appropriate? Do you agree that the outcomes should also include a resolution-focused requirement? Please explain.</p> <ul style="list-style-type: none"> ▪ As stated above, WNZL welcomes the Reserve Bank retaining the focus on outcomes to enable flexibility to meet the required outcomes in a way that suits the particular circumstance and business model of the bank. However, WNZL considers it is already meeting the Reserve Bank's outsourcing policy objectives and therefore does not see the need for the imposition of a new set of prescriptive outsourcing requirements. The policy objectives of BS11 could instead be made clearer and the Reserve Bank could undertake further monitoring of banks' compliance with them. WNZL considers that the statement in paragraph 46 that "<i>Large Banks tended to focus on business continuity involving a natural disaster or technology failure</i>" does not apply to its approach to BS11. WNZL is aware of the need for the bank to continue to operate on an ongoing basis post a failure event and takes this into consideration when entering into any BS11 core function outsourcing arrangements both with its parent bank and other outsourcing providers. ▪ The Consultation Paper notes that the stocktake of Large Banks' compliance with the outsourcing policy found that banks' interpretations of what functions should be defined as core for the purposes of the policy varied. This may have resulted from a lack of key definitions and clarity in the current policy. ▪ The Reserve Bank is proposing to replace the existing "<i>core functions</i>" in BS11 with the outcomes set out in paragraph 49. As set out in Section 3 of this submission, WNZL proposes that the policy retain the concept of Core Functions. Drawing on the Reserve Bank's policy objectives identified in paragraphs 49 and 55 of the Consultation Paper, WNZL proposes that the Core Functions be defined as follows: <ul style="list-style-type: none"> ○ meeting the bank's daily clearing/interchange and counterparty settlement obligations (note that the reference to "<i>other time-critical obligations</i>" has not been included as it does not appear to add anything). ○ understanding the bank's credit, market and liquidity risk positions. ○ having access to relevant systems and balance sheet data to enable the bank to calculate its financial position and undertake its prudential regulatory reporting. ○ the provision of basic banking services to existing customers. ▪ The OBR Policy appears to contemplate that basic banking services include: <ul style="list-style-type: none"> ○ consumer and small business customers having access to their transaction accounts, that is, being able to make deposits and withdrawals, to service their existing loans and other basic credit facilities, to apply for new credit, and to provide account activity reporting; ○ in terms of channels, access only to branches, ATMs, and online banking; and ○ in terms of payment instruments and methods, access to cash, debit cards,

	<p>credit cards, and direct credits.</p> <ul style="list-style-type: none"> ▪ Specific comments on the outcomes in paragraph 49 are as follows and have been reflected in the amendments to the Core Functions set out above: <ul style="list-style-type: none"> ○ Paragraph 49(c) – This outcome links systems and balance sheet data with the availability of a range of options for managing the failed bank. However, it is unclear what may be required of a bank in order for those systems and data to provide "a range of options" for managing the bank. It is also unclear what the term "at hand" means. ○ Paragraph 49(d) – "basic banking services" needs to be defined. In order for a bank to comply, there would need to be a clear understanding across the industry about what constitutes <i>basic banking services</i>. ○ A bank might have systems in place or offer certain products or services which although relevant in some way to a Core Function, would be regarded as having an indirect or immaterial impact, as opposed to others which might be critical to the delivery of that Core Function. For example, a bank might: (i) offer specific customers a product with unique operational requirements but which would otherwise fall within the definition of basic banking services; or (ii) have a large number of minor or supporting 'utility level' applications with indirect connectivity to a Core Function system. Without any materiality threshold, these applications, products and services could fall within the ambit of the policy. They should not be included in the Required Operational Outcomes. ○ Paragraph 49(e) – The stated outcome is not of itself a function but rather more of an expectation that the outcomes in (a) to (d) are able to delivered on an ongoing basis. It refers to a bank being able to operate on this basis as a stand-alone entity every day thereafter. This does not appear to be an outcome but rather a requirement that the bank can keep going. In the proposed Policy Framework it is covered by the reference to timeframes which reflect the requirement in the current policy to deliver the functions on an ongoing basis.
<p>Q6</p>	<p>Do you agree that the matters identified above are the appropriate matters for inclusion in a separation plan? Are there any matters that have not been identified above, but should be included?</p> <ul style="list-style-type: none"> ▪ If the Reserve Bank's proposal to prohibit certain functions from being outsourced to related parties proceeds, it is not evident that a separation plan will be required as a bank will be required to have its own systems to deliver the functionality referred to in paragraphs 55(a) and (b). However, on the assumption that the Reserve Bank continues to allow outsourcing of the prohibited functions to the bank's parent or a related party, the requirements of the separation plan should: <ul style="list-style-type: none"> ○ map to the required outcomes from the outsourcing policy; ○ not be a requirement imposed by a condition of registration; ○ not deal with an abrupt loss of service; and ○ not be required to be approved by a bank's Board of directors. ▪ The separation plan should cover the outcomes that will be required by the policy. Although there is some overlap in the requirements listed in the outcomes in paragraph 49 and the contents of the separation plan in paragraph 55, they are not

	<p>identical. Items (a) and (b) cover some of the same matters but there are differences between them that do not appear to have been intentional.</p> <ul style="list-style-type: none"> ▪ Clarification is also required in relation to requirement (c) of paragraph 55. It is not evident what is intended by the reference to "<i>manage the operational responsibilities for the separation</i>". ▪ Paragraph 55(d) specifies that the bank should have parallel rights for functions outsourced through the parent or a related party. WNZL considers that a bank should have the freedom to determine what is the most appropriate way to ensure critical services continue to be made available post separation (including from a third party provider). This may not involve having parallel rights as there may be other more appropriate legal and practical options available. In addition, the policy should make it clear that only functions that are in scope of the policy will need to continue post separation. Paragraph 55(e), which refers to the separation plan setting out robust alternative arrangements for systems that are owned or controlled by the parent or related party, should also be limited in this manner. ▪ WNZL has had a bank separation plan for a number of years which has been tested annually in an invocation test scenario. Despite there being no current policy requirements relating to separation, these arrangements have worked well largely due to there being flexibility with respect to them. The plan can be adapted to accommodate changes to parent bank outsourcing arrangements. WNZL therefore queries the need for a requirement for a separation plan being included as a condition of registration and the level of prescription that is proposed with respect to that requirement. The compliance burden of having a separation plan will significantly increase if there is a risk that a bank may be non-compliant with its conditions of registration if it fails to make what may be an immaterial change to its plan ▪ The separation plan should only deal with the scenario where there is a failure of the parent bank itself (or a related party) and not with an abrupt loss of access to functions provided by those parties for an indefinite period. While it can be expected that there will, from time to time, be a loss of some functionality provided by those parties to the New Zealand bank, loss of all services for an indefinite period of time is unlikely because of the parent bank's DR and business interruption event contingency arrangements. Separation in those circumstances would not be appropriate and the plan should not be required to deal with this scenario. ▪ The separation plan should not need to be approved by a bank's Board as it is an operational risk document, which has some similarity to a BCP. The Board's focus should be on ensuring that a robust separation plan is in place rather than engaging on the detail of the document.
Q7	<p>Does the proposed definition appropriately define outsourcing? If not, please provide an alternative definition that, in your opinion, better captures what is meant by the term outsourcing.</p> <ul style="list-style-type: none"> ▪ The proposed definition of outsourcing is not regarded as appropriate as it is too wide and goes beyond what is normally considered to be outsourcing and the scope of the relevant provision in the RBNZ Act. Rather than focusing "<i>the range of issues that would potentially be relevant for the policy</i>" the proposed definition expands it so that its scope includes all types of supply and procurement arrangements. WNZL has set out a suggested alternative definition of outsourcing in Section 3 of this submission

	<p>but sets out below its concerns with the definition proposed.</p> <ul style="list-style-type: none"> ▪ The definition is described as a modified version of the Basel Committee’s definition but one key difference is that the Basel Committee’s definition refers to activities that "<i>would normally be</i>" undertaken by the bank rather than those activities that "<i>could be</i>" undertaken by the bank. The Basel Committee’s definition is more consistent with the usual, commercial understanding of what outsourcing involves. While a bank could potentially undertake a number of activities (subject to its condition of registration restricting non-financial activities to activities that in aggregate are not material) the definition should refer to activities that would normally be undertaken by a bank. The reference to "<i>could</i>" makes the definition unlimited and extends the ambit to cover activities that are not within a bank’s core business or capability. The definition could apply to general supply arrangements that would normally be regarded as procurement. This is another key distinction with the Basel Committee as it excluded "<i>purchasing contracts</i>". ▪ The Reserve Bank’s authority to regulate outsourcing derives from s78(1)(fb) of the RBNZ Act. That paragraph refers to "<i>arrangements for any business, or functions relating to any business, of the applicant or registered bank to be carried on by any person other than the applicant or the registered bank</i>". The proposed definition does not appear to capture the fact that the activities which are outsourced must relate to the business of the bank that is doing the outsourcing. In recent discussions with Reserve Bank staff they indicated that they considered [REDACTED] <p>[REDACTED]</p> <p>The definition should not be expanded in this manner so that it includes arrangements whereby a bank markets or sells another entity’s products. [REDACTED]</p> <ul style="list-style-type: none"> ▪ The broadened definition would have a significant flow-on effect on operational and resourcing requirements and compliance costs as, under the current proposals, it impacts on what must be included in the proposed compendium and notified to the Reserve Bank. ▪ While the definition proposed is not regarded as appropriate, it is possible to have a broad definition of outsourcing but restrict the ambit of the outsourcing policy so that it applies only to arrangements that are relevant. Both the Basel Committee and APRA’s CPS 231 take into account the materiality of arrangements. WNZL’s proposed policy framework set out in Section 3 would limit the scope of the policy so that only arrangements that are relevant to the policy outcomes would be in scope. In contrast, the only exclusions proposed in the Consultation Paper are the matters listed in paragraph 62. The result is that the new requirements which are proposed would apply to all contracts that are regarded as "<i>outsourcing</i>", regardless of their significance to the business or the resolution scenario.
Q8	<p>Are there any other functions that should be excluded from the outsourcing policy, but are not captured in the list above?</p> <ul style="list-style-type: none"> ▪ WNZL considers that rather than having a <i>white list</i> of items that are not captured by the definition of outsourcing, the outsourcing policy should apply only to Core Functions and a materiality threshold should be applied.

	<ul style="list-style-type: none"> ▪ One of the risks of the white list is that there is no distinction between general business supply services and procurement and what is genuine outsourcing. A bank may regard a supply arrangement as procurement and consider it not within scope of the policy, but the Reserve Bank could deem it to be outsourcing and regard the bank as being non-compliant for failing to notify the Reserve Bank of the arrangement. ▪ In addition, there are likely to be many business services, activities and functions that will not have been included on the list but that should have been and as the industry evolves there will be additional items that will need to be included. Banks will be required to engage with the Reserve Bank on an ongoing basis about any items that are not on the list at the time the final policy is published. ▪ If the white list approach is retained, at a minimum, the following matters should be added to it: <ul style="list-style-type: none"> ○ Licences for generic, non-customised software and the maintenance and support of that software ○ General office products and consumables ○ Corporate uniforms ○ Furniture, fittings and furnishing ○ Commercial and office building construction services ○ Interior finishing and furnishing and remodelling services ○ Courier services ○ Document storage, archiving, destruction and deeds management services ○ Rental property leases ○ Recruitment services ○ Reference and background check services ○ Title search and security/collateral registration services ○ Real estate appraisal and valuation services ○ Sponsorship, brand or promotional arrangements ○ Promotional or advertising printing ○ Debt collection ○ Predictive dialler and automated voice recording services ○ Catering services ○ Accommodation services ○ Meeting facilities ○ General business utility services ○ Security system, premises access and guarding services ○ Fraud and forensic detection services ○ Agency and trustee arrangements for treasury programmes and syndicated loan facilities
--	---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------

	<ul style="list-style-type: none"> ○ Custodial funds management services ○ Share, domestic note and bond registry and management services ○ Locked box and electronic mail capture services ○ Sales, promotional and direct marketing activities ○ Data mining, customer surveying and rewards programmes ○ Credit reporting services ○ Property and facility maintenance services ○ Clearing and settlement arrangements between members or participants of clearing and settlement systems ○ Credit card scheme providers. <p>▪ The list of functions outlined in paragraph 62 should also be expanded to cover other matters. For example, printing services should apply more widely than simply to the printing of marketing materials, and advisory and consulting services should cover all professional and specialist advisors and services.</p>
Q9	<p>Do you agree that there are functions that are so integral to carrying on the business of a bank that they should not be outsourced?</p> <ul style="list-style-type: none"> ▪ WNZL does not consider it appropriate that there be a blanket prohibition on outsourcing specific functions. Banks should be allowed to achieve the outsourcing policy objectives in the most optimal way. Provided a bank is able to demonstrate that its outsourcing arrangement solutions meet the policy objectives then that should be sufficient to meet prudential requirements as it allows the bank to organise its affairs in a manner which minimises compliance and operational cost. ▪ Banks are in the business of assessing and managing risk across a number of key functions, including credit, liquidity, market and operational risk. Risk assessment is a fundamental bank undertaking and WNZL considers that it is entirely appropriate that banks be trusted to assess, mitigate and manage supplier/outsourcing risk in the same way other risk factors are managed. ▪ Supplier risk is captured within the overall operational risk construct and can be appropriately managed by the bank under the auspices of risk governance frameworks, tools and operational processes. As a key component of broader operational risk assessment, banks are well placed to assess and consider both third party and related entity outsourcing risk – from the governance, strategic, operational and customer impact perspectives. ▪ Bank risk functions are comprised of people with decades of collective skill and experience in risk identification and management, and this capability is supported by highly specialised technology, business, legal and commercial management expertise. WNZL considers that this collective competency is the appropriate body to be assessing and managing outsourcing risk on an individual function and supplier basis, rather than there being a blanket prohibition on outsourcing certain functions. ▪ This approach enables the bank’s experts to consider and balance all risks arising from any proposed outsourcing (both supplier and other operational risks) and, if deemed acceptable based on agreed risk appetite and parameters, to ensure that the requisite legal and practical risk mitigants are deployed to effectively minimise and

manage that risk.

- The prohibition on outsourcing certain activities runs counter to accepted global system and capability modelling. For example, most global banking risk models rely on a centralised area of speciality which maintains model methodology and critical system oversight and maintenance which is then leased out to the regions in which the bank operates. This is accepted by international regulators and the banking industry as good practice. Centralisation has not been raised as a concern by global regulatory bodies or in any Basel edicts.
- If the use of a centralised hub of expertise and systems were prohibited, WNZL considers that this would significantly increase risk, and impact global regulatory reporting and compliance requirements. The prohibition would result in current synergies and benefits of global platforms, systems and capability being lost, and would result in a number of adverse impacts to the business, customers and markets. The impacts are set out in detail in the Attachment, and include:
 - a reduced ability to leverage parent bank capability;
 - higher costs to customers as a result of the loss of diversification benefits and inefficiencies caused by the need to replicate systems and processes;
 - a reduction in the ability to effectively monitor, report and analyse risk exposures by accessing specialised global applications and capability which deliver consistency of approach and outcomes for risk management across the banking group;
 - the introduction of inconsistencies in calculations computed from differing or replicated systems which use the same sets of data, which creates a lack of consistency and reliability in information (This could adversely affect the banking group's ability to meet global regulatory obligations and internal monitoring requirements, and would unnecessarily increase investigation and resolution times relating to the data discrepancies.); and
 - an increase in operational and technology risk by duplicating systems in an already complex technology environment, and the need to interface these systems to a number of other local and global systems and applications.

Do you agree that these examples are appropriate? Are there any other functions or systems that should not be outsourced?

- No. The Reserve Bank is proposing that certain functions be prohibited from being outsourced given their importance in achieving the objectives of the outsourcing policy. A bank should be permitted to outsource these functions to a related party where it has appropriate BCP arrangements in place to deliver the required policy outcomes in a failure event.
- The examples the Reserve Bank provides are systems used to calculate the daily financial position, SWIFT gateway and licences supporting transaction processing, and data required for regulatory reporting. The Reserve Bank's basis for the proposal stems from concern that:
 - some current workarounds that banks have in place are effectively just DR for the parent bank system; and
 - back-up options for parent systems may not be sustainable post separation, as they are focused on returning the parent system to operation and not on longer

term continuity of the New Zealand bank's operations.

- WNZL does not consider these concerns are warranted as they do not make a distinction between DR and BCP arrangements. While DR arrangements may not be appropriate to deliver the required functionality, this does not mean that BCP arrangements are not appropriate.
- DR is the backup technology process invoked when the parent bank is working to bring the system back up following a significant outage. This is not a contingency arrangement for the New Zealand bank, but is the first port of call for remediation on a business as usual basis, i.e. the parent bank is not facing any sort of stress event, there is just a system issue.
- BCP, workaround or contingency provisions are where the New Zealand bank has put arrangements in place for its own alternative operational capability, which can be invoked in the event of a prolonged parent system outage (refer to paragraph 3.11(d) above) or on failure.
- Contingent arrangements are alternative systems, channels or functions which enable the New Zealand bank to function independently of the related entity in the event that the outsourced function is no longer available. These arrangements are robust alternative pathways for getting to the same required outcome – and may be a combination of a backup onshore systems, pre-licensed and configured third party applications, automated processes capturing data, reporting and calculations, or a combination of these options.
- The contingent arrangements are documented and managed in accordance with standard business continuity and incident management policies and processes and are owned by the executive responsible for the underlying business function or outcome. They are regularly tested to ensure that they are fully operational and functional in order to deliver continued and sustainable operability of functions.
- Contingency arrangements are developed on the basis they will be the primary mechanism or channel to enable the outsourced function or service to be delivered with minimal adverse customer impact or disruption to business operations. They are prepositioned and tested arrangements that can be deployed on a priority basis in both prolonged outage and stress scenario environments, ensuring the bank retains the capability to capture or replicate any inflight payment transactions or material intraday position data, as well providing operational functionality for the bank going forward.

- [REDACTED]
- [REDACTED]
- [REDACTED]

	<p>[REDACTED]</p> <ul style="list-style-type: none"> ■ [REDACTED] ■ [REDACTED] ■ [REDACTED]
--	------------------------------------------------------------------------------------------------------------------------------

Q10	<p>Do you think an outsourcing arrangement compendium would be useful as a reference record between the Reserve Bank and a bank?</p> <ul style="list-style-type: none"> ▪ WNZL agrees that a tool facilitating visibility of a bank’s outsourced functions is appropriate but does not agree that it must be a compendium requirement. WNZL proposes a requirement that the bank must instead be able to generate a report of all contracts in respect of its outsourced functions from an Outsourcing Arrangements Repository (refer paragraph 3.14 above). ▪ The Outsourcing Arrangement Repository requirement (rather than a mandatory compendium) would minimise inefficiency and unnecessary cost by permitting a bank to use its existing contracts database (modified if required) or choose a tailored contract management tool that would allow the bank to achieve the same outsourcing policy outcome, but not result in duplication of existing contract management functionality. As banks already use contract databases for their commercial and supplier management, they have sound business, legal and operational reasons for maintaining them in an up-to-date and accurate state. ▪ A centralised Outsourcing Arrangements Repository would be capable of generating a report of the bank’s outsourcing contracts. [REDACTED] ▪ This data would be available to a statutory manager in a failure event, and together with business information from the bank’s heads of procurement and legal and other senior management, would provide an immediate and accurate picture of the key supply arrangements. ▪ In addition to concerns about the duplication and inefficiencies created by the use of a mandatory compendium (as opposed to an Outsourcing Arrangements Repository) we note that a compendium could be out of date by the time it is delivered to the
-----	-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------

	<p>Reserve Bank. This is because it would take time to have it agreed and signed off internally prior to submission. During that time other contracts could have been amended, renewed and entered into.</p> <ul style="list-style-type: none"> ▪ A significant amount of resource would be required to maintain the compendium and manage the continuous updates being provided to the Reserve Bank. Unlike the compendium of liabilities required for compliance with the OBR policy, and the compendium of capital models, required under the Capital Adequacy Framework for Internal Ratings banks, a compendium of all outsourcing arrangements would, under the current proposal, contain [REDACTED] ▪ Imposing a compendium requirement by means of a condition of registration also has the potential to result in non-compliance solely because a contract has been omitted, either by human error or because the bank had misinterpreted whether the contract came within the definition of outsourcing. Any condition of registration would also need to take into account the fact that the compendium would require constant amendment so it may not be accurate at different points in time. ▪ If a compendium requirement is deemed to be necessary, it should be confined to the functions captured within the Scope of Outsourcing (refer paragraph 3.3 above), to ensure that non-material general procurement and supply contracts are excluded. WNZL considers that the cost and operational impacts for a bank to provide this level of detailed information in a compendium would exceed the benefit to a statutory manager. ▪ The Consultation Paper refers to the compendium being "<i>a key accountability document</i>" and that it "<i>should be embedded in board compliance</i>". It further states that it should be "<i>updated, and form part of the oversight and governance reviews undertaken by the board and senior management</i>". It is not clear what the Reserve Bank's expectation is with regard to Board engagement. If the Reserve Bank imposes the compendium requirement as a condition of registration the directors will be required to attest that the bank is compliant, just as they do with other conditions of registration. The bank would put in place appropriate controls for this requirement as it does for other conditions of registration. However, the Board should not be expected to engage with the document itself as this would not be an appropriate use of the Board's valuable time.
Q11	<p>Are there any other matters not addressed above that should be addressed in the compendium?</p> <ul style="list-style-type: none"> ▪ Paragraph 78 refers to the compendium including the expiry or renewal date of the contract but Appendix two, which lists the details of the outsourcing arrangements to be included in the compendium, does not contain a column for that information. It is acknowledged that if there is to be a compendium requirement, the date of the expiry of the contract would be useful information.
Q12	<p>What are the costs to you of establishing and maintaining an outsourcing arrangement compendium that forms part of your conditions of registration?</p> <ul style="list-style-type: none"> ▪ WNZL already maintains a contracts database to manage commercial and supplier arrangements and would continue to do so if a compendium were required.

	<ul style="list-style-type: none"> ▪ Establishing and maintaining a compendium would duplicate the bank's current contract management operations and costs, and would result in a significant amount of additional resourcing being required for the initial transfer of [REDACTED] contract entries and for ongoing compliance requirements. ▪ Assuming that the compendium would not be limited to the functions captured by the Scope of Outsourcing (paragraph 3.3 above), it would require significant resourcing to: produce and maintain it; manage the internal review and sign off process; submit the compendium to, and engage with, the Reserve Bank on the arrangements; and amend and re-submit the compendium if changes were required as a result of Reserve Bank feedback. ▪ The current proposal is that the compendium would need to be updated for any new outsourcing arrangements or changes to service providers. [REDACTED]
<p>Q13</p>	<p>Do you agree that all contracts for outsourcing arrangements should be required to include the terms outlined in paragraph 81?</p> <ul style="list-style-type: none"> ▪ WNZL has two key concerns with this proposal. ▪ The first is that, as noted in Section 3 above and question 10, the proposed scope of the policy is too broad and will capture contracts relating to matters outside the proposed Scope of Outsourcing. As set out in the Key Submissions, the policy should be restricted to outsourcing arrangements that are relevant to achieving the policy's objectives. ▪ The second concern is that, even if the scope of the policy is modified as proposed, not all the contractual terms proposed may be suitable for every arrangement. It is not considered appropriate that there be a definitive list of non-negotiable (and not clearly defined) contractual terms required to be applied generically to all supply contracts. ▪ Paragraph 81 of the Consultation Paper states: "<i>Given the importance of ensuring outsourcing arrangements are robust and that functions outsourced to independent third parties, and arrangements made through the parent or a related party, will remain available following a failure we propose to require certain terms and conditions that an agreement must contain.</i>" WNZL does not accept this rationale as we consider that only some arrangements will engage the policy concerns outlined in the Consultation Paper. ▪ Banks enter into a large number of business as usual outsourcing arrangements and in many cases, if those service providers were to fail, the functions that would be disrupted or the costs that would be incurred as a result would not be sufficiently serious to "<i>threaten the bank's survival to the extent that the soundness of the system was at risk</i>" (or at all). Those arrangements would not therefore require the mandatory contractual provisions referred to in paragraph 81 and Appendix one. ▪ If, as proposed in paragraph 81, there is a requirement that all contracts contain provisions ensuring:

	<p>(a) continued access on normal commercial terms to service when the bank enters statutory management;</p> <p>(b) that the Reserve Bank has access to the documentation and information (noting it is not clear what "access" involves); and</p> <p>(c) that parallel rights exist for arrangements made through the parent, there will be:</p> <p>(d) a significant cost and time impact in negotiating provisions that are unnecessary for contracts of a non-material nature and that would be deemed unacceptable contractual provisions to a significant number of suppliers, particularly global suppliers; and</p> <p>(e) a significant impact on the overall supplier engagement process due to the increased time and legal costs incurred by both the bank and the supplier.</p> <ul style="list-style-type: none"> ▪ The same argument applies to the list of contractual terms set out in Appendix one. While most of these terms would be suitable for <i>material</i> outsourcing arrangements, they will not be required in all cases, nor will those terms always be agreed by counterparties in which case other mitigants may be required. ▪ It is also not clear from the list provided at Appendix one exactly what restrictions, prohibitions or obligations banks would be expected to include in relation to each contractual term. While the list sets out broad topics, it does not give any indication as to how these requirements should be approached. The high-level nature of the '<i>expected provision</i>' headings does not provide detail as to the nature or extent of the actual contractual condition that is envisaged by the Reserve Bank. ▪ For example, "<i>the scope of the arrangement and services to be supplied</i>", "<i>pricing and fee structure</i>" and "<i>insurance</i>" are standard provisions that are covered in all WNZL's contracts. They are negotiated and approved by WNZL's contracts legal team and sourcing specialists. It is therefore unclear what, if any, additional requirements the Reserve Bank would be seeking to impose. ▪ In terms of Appendix one, there are other contractual terms proposed that would require further clarification as they are open for interpretation. For example: <table border="1" data-bbox="403 1386 1430 1926"> <tr> <td data-bbox="403 1386 917 1715">c. escrow arrangements</td> <td data-bbox="917 1386 1430 1715">Escrow provisions would not be appropriate (or acceptable to suppliers) in all software arrangements. Provisions would usually only be appropriate in relation to the provision of certain non-generic, tailored software that required significant ongoing support from the supplier.</td> </tr> <tr> <td data-bbox="403 1715 917 1845">d. review provisions</td> <td data-bbox="917 1715 1430 1845">It is unclear what type of provisions the Reserve Bank is envisaging in relation to <i>review</i> requirements.</td> </tr> <tr> <td data-bbox="403 1845 917 1926">p. insurance</td> <td data-bbox="917 1845 1430 1926">It is unclear whether the term <i>insurance</i> is referring to supplier or</td> </tr> </table> 	c. escrow arrangements	Escrow provisions would not be appropriate (or acceptable to suppliers) in all software arrangements. Provisions would usually only be appropriate in relation to the provision of certain non-generic, tailored software that required significant ongoing support from the supplier.	d. review provisions	It is unclear what type of provisions the Reserve Bank is envisaging in relation to <i>review</i> requirements.	p. insurance	It is unclear whether the term <i>insurance</i> is referring to supplier or
c. escrow arrangements	Escrow provisions would not be appropriate (or acceptable to suppliers) in all software arrangements. Provisions would usually only be appropriate in relation to the provision of certain non-generic, tailored software that required significant ongoing support from the supplier.						
d. review provisions	It is unclear what type of provisions the Reserve Bank is envisaging in relation to <i>review</i> requirements.						
p. insurance	It is unclear whether the term <i>insurance</i> is referring to supplier or						

		<p>bank insurance, and what matters in relation to the arrangement the Reserve Bank would expect to be insured.</p>
<p>Q14</p>	<p>Do you agree that option two is the most appropriate option for the assessment of outsourcing arrangements? Please explain.</p> <ul style="list-style-type: none"> ▪ WNZL notes that the commercial negotiation process is tailored to ensure each contract adequately addresses the nature of the service or function being outsourced and the specific risks and business requirements relevant to the individual supplier and arrangement. In any contract negotiation for the provision of services, there are certain <i>boilerplate</i> terms and conditions the bank will seek to obtain. However, these always need to be considered on an individual basis to ensure they are an appropriate fit for the arrangement being entered into – including addressing any identified commercial, legal and regulatory risks (refer question 15 for further commentary on the risk assessment process). <ul style="list-style-type: none"> ▪ WNZL considers that engagement options one and two will both give rise to significant resourcing, cost and business operational implications for banks. As noted in question 9, WNZL considers that it would be more appropriate for banks to undertake the requisite risk assessment and due diligence of their arrangements (on the basis of the governance and operational frameworks) to ensure they meet the requirements of the outsourcing policy, as occurs with other condition of registration compliance. Banks should be able to seek the Reserve Bank’s advice where the assessment process raises any uncertainty or where they need some assurance before investing in a significant outsourcing arrangement. In those situations, the expectation is that the Reserve Bank would provide written reasons for its decision, which a bank could rely on. ▪ The Reserve Bank will be able to monitor banks’ compliance by requesting the BS11 assessment for any in-scope outsourcing arrangement. This monitoring will also allow the Reserve Bank to assess whether banks are adopting a consistent approach to the interpretation of the policy. ▪ If a notification to the Reserve Bank were regarded as necessary, we consider it should not apply to all outsourcing arrangements, but should be restricted to arrangements that relate to a Core Function and only where they are material as set out in the Proposed Policy Framework in Section 3. ▪ The Consultation Paper points to the lack of any formal Reserve Bank engagement process on outsourcing as having led to variable BS11 outcomes across the industry. However, it is not clear that lack of engagement is the main reason for that variability as it is likely that banks’ uncertainty about the current BS11 policy scope has also contributed. ▪ WNZL notes the proposed notification requirements represent a major shift from the emphasis on the self-discipline pillar to the regulatory discipline pillar and with it an increase in moral hazard. In other areas the Reserve Bank usually relies on directors to attest to compliance with the bank’s conditions of registration without the requirement to engage with the Reserve Bank on the operation of the condition of registration. 	

- The broad scope of the current proposals would make both options very difficult to administer due to the significant volume of arrangements captured (refer to questions 10 and 12 for WNZL's indicative numbers).
- To ensure the process is more manageable for the Reserve Bank and banks, we suggest that any notification or non-objection requirement should apply only to the much more limited arrangements identified in Scope of Outsourcing in Section 3 above.
- If the proposed Scope of Outsourcing limitation is not applied to the notification or non-objection requirements, we anticipate that the volume and content of the submissions that banks would need to make to the Reserve Bank could make the process largely unwieldy and would necessitate sufficient Reserve Bank resourcing to cope with the capacity.
- As noted in Section 3 and question 9, we consider that sound risk frameworks, policies and processes and accurate contract record keeping are the appropriate mechanisms to ensure BS11 compliance.

Option Two – Impacts and Suggested Amendments

- Although WNZL considers both options would be operationally problematic, option two would be preferable to option one, but some amendments would be of assistance to make the proposal more workable for banks.
- The main concerns with option two relate to the timing of Reserve Bank engagement and response and with the scope and impact of the non-objection process. The key matters for further consideration are:
 - (a) Timing of response – the Reserve Bank's assessment process would ideally need to be less than three weeks. While option two is expected to be faster if the Reserve Bank does not require a non-objection notice, we anticipate it would likely be longer where that is the case. Under the current proposal, a bank would be unable to sign a contract or commence the underlying commercial arrangement for at least twenty working days or until the receipt of the non-objection notice. This would impact on the bank's commercial activity and restrict business flexibility and nimbleness.
 - (b) Notification process – the notification process should ideally involve a two tier approach. Contracts falling within the first tier (those captured by the Scope of Outsourcing) would require oversight, being either a Reserve Bank non-objection notice or notice of arrangement to the Reserve Bank, and the second tier (those outside the Scope of Outsourcing) would not require any further action. Such a tiered approach would facilitate the Reserve Bank's stated objective of striking: *'a balance between ensuring that the Reserve Bank has oversight of the outsourcing arrangements that banks are entering into... while allowing for banks to enter into arrangements that have little impact on the objectives'*.
 - (c) Timing of engagement – the timing of the Reserve Bank engagement process would adversely impact on the commercial management process and it would

be preferable if engagement occurred prior to the final documentation stage. For both options one and two we note that engagement with the Reserve Bank seems to be contemplated once the contract has been finalised or is close to being finalised. With option one, the bank must have involved the Board or a senior manager in approving the agreement, which would normally be done at a late stage in the process once key terms were agreed. Similarly, for option two, the bank is required to provide the expiry or renewal date of the contract, which would only be known once the contract terms had been finalised.

(d) Assessment process outcome – if the bank is awaiting the assessment process outcome, there will be cases where the contractual terms cannot be finalised with the supplier. This gives rise to several practical and business implications:

- Once a contract is at the stage where it is ready to be signed, the bank and the supplier will have invested significant business, commercial management and legal resource in getting it to that stage. [REDACTED]

[REDACTED] For a major agreement, the bank would have spent a considerable amount of time negotiating the contract terms, including the BS11 related ones.

- Suppliers may not wish to contract with a New Zealand bank because of the risk of the regulator objecting to the agreement at a late stage after the supplier has invested significant time and cost.
- Negotiations with major suppliers can extend over several months, particularly where the counterparty is a global entity with senior management and external counsel in other jurisdictions, as New Zealand legal, tax and regulatory requirements can take a significant amount of time to work through.
- Where the arrangement is one that involves the introduction of a new product or service for customers, the bank would be unable to plan for the launch until the expiry of 20 working days, or an even longer period where a non-objection was subsequently required. [REDACTED]

- Until the Reserve Bank's final decision was known, the bank would be required to effectively put all marketing, customer and internal communications, change management and operational planning and programming on hold, which would be operationally undesirable.
- Where the outsourcing arrangement involved regulatory or legislative compliance, the bank's compliance could be put at risk while the bank waited for a response. The possibility that the Reserve Bank might, at a late stage in the project, prohibit the bank from entering into the arrangement could result in the bank being non-compliant while it looked for an alternative solution.
- It would be uncommercial for a bank to spend a significant amount of time and money on developing a product, project or system through to contract

	<p>execution stage to risk being told by the regulator that it would not agree to the arrangement or that the bank needed to re-open negotiations because the contract terms were deemed unacceptable</p> <ul style="list-style-type: none"> ▪ To address the option two process issues noted above, we suggest that the engagement (on arrangements within the Scope of Outsourcing - tier one) needs to take place at an early stage to avoid the problems noted above of committing time, cost and resources to a project that may ultimately not proceed. ▪ This initial engagement is anticipated to include a high level overview of the proposed outsourcing, the identified business risks and impacts and a discussion of the controls that the bank is likely to seek in the proposed arrangement. ▪ To enable the bank to efficiently manage the commercial process with the supplier, the policy should provide sufficient flexibility for a bank to carry out its commercial negotiations, including determining what legal and practical controls are deemed appropriate as risk mitigants. This would recognise that a generic approach to contract negotiations is not feasible, and that a bank may not be successful in obtaining all the controls it seeks. It would also allow the bank's considerable internal and external legal and commercial management expertise to assess whether the level of legal risk is acceptable. ▪ It would be of assistance to have more detail about the Reserve Bank's process for considering outsourcing arrangements and what appeal rights a bank would have if the bank disagreed with the Reserve Bank's determination.
<p>Q15</p>	<p>Do you agree that the approach outlined above is an appropriate way to manage the assessment of outsourcing proposals? If not, please explain.</p> <ul style="list-style-type: none"> ▪ As noted in question 9, WNZL is of the strong view that the appropriate entity for considering outsourcing risk is the bank itself, as it has the requisite expertise. However, under the policy proposal, both options involve all of a bank's outsourcing arrangements being subject to Reserve Bank scrutiny. ▪ Under the proposed outsourcing proposal process, the Reserve Bank will be making determinations on supplier risk relating to matters such as cutting edge banking products, complex technology projects and highly specialised payment facilities. Considering the bank that has developed the product, project or initiative and assessed its impact and risks has had the benefit of considerable expertise – including technology, payments, business operations, legal and commercial management subject matter experts – WNZL is concerned that the Reserve Bank has significantly underestimated the specialist resource required to enable any meaningful assessment of a proposed outsourcing arrangement. ▪ While these arrangements will in some way involve a supplier of systems or services which will trigger the Reserve Bank's outsourcing risk review, this risk is only one of a number of key risks that need to be considered with any new product, project or initiative. These other risks need to be effectively and appropriately balanced against outsourcing risk, so that supplier risk mitigation is not disproportionately emphasised at the expense of other operational, market and business risks. ▪ As stated above, the Reserve Bank's scrutiny should be restricted to outsourcing arrangements that have the potential to affect the objectives of the policy. Those arrangements that have little or no impact on the objectives should not have to be

	<p>submitted to the regulator prior to the bank entering into them.</p> <ul style="list-style-type: none"> ▪ If all "outsourcing" arrangements are caught by this requirement it is estimated that the Reserve Bank will be required to consider possibly [REDACTED] contracts per annum from the industry. This will be a significant impost on the Reserve Bank's resources. ▪ The Reserve Bank has not provided an estimate of how long it will take to provide a bank with a notification about whether an arrangement will require "non-objection" nor has the Reserve Bank provided an estimate of how long the non-objection process will take. It is therefore difficult to assess the likely impact this proposal may have on banks' operations.
Q16	<p>Do you agree that having standardised applications would assist in reducing the time taken to assess outsourcing proposals?</p> <ul style="list-style-type: none"> ▪ Yes, although WNZL does not consider that there should be a formal notification requirement as proposed.
Q17	<p>How many requests per annum do you expect to file in a business-as-usual state? How many requests do you expect to file at the outset of the policy?</p> <ul style="list-style-type: none"> ▪ [REDACTED] ▪ [REDACTED]
Q18	<p>Do you think that the threshold for the outsourcing policy should be aligned with the threshold for OBR pre-positioning, given the inter-linkages of the two policies?</p> <ul style="list-style-type: none"> ▪ The threshold for the outsourcing policy should not be aligned with the threshold for OBR pre-positioning. ▪ When designing regulatory policy, the size of the New Zealand market and the size of the banks operating in that market must be taken into account. [REDACTED] ▪ [REDACTED] ▪ [REDACTED] ▪ Relative to the size of New Zealand's banking industry the threshold of \$1billion is not

<p>Q19</p>	<p>Do you agree that 6 months is an appropriate amount of time for banks to provide the Reserve Bank with a plan for how it will come to compliance with the revised outsourcing policy, noting that its form has not yet been finalised?</p> <ul style="list-style-type: none"> ▪ While it is not possible to assess how much time will be required for a bank to draft a plan to comply with a revised outsourcing policy until the content of the policy is known, based on the proposals in the Consultation Paper, six months is expected to be inadequate. ▪ The time required will depend on the shape on the final policy but WNZL considers that a more realistic timeframe would take between [REDACTED] ▪ [REDACTED] ▪ [REDACTED] <ul style="list-style-type: none"> ▪ [REDACTED] ▪ [REDACTED] ▪ [REDACTED]
<p>Q20</p>	<p>Do you agree that 2 years would provide a sufficient timeframe to reach compliance with the policy?</p> <ul style="list-style-type: none"> ▪ WNZL considers that two years would be inadequate to reach compliance with the policy (based on the Reserve Bank’s proposed policy), but notes that the time required will depend on the final policy decisions. ▪ Our considerable experience with major technology projects has shown that two years is the minimum amount of time required for any significant technology project or system change. Where there are multiple system changes that need to occur (as would be the case with the current proposals), the project complexity and operational risk that needs to be carefully managed increases. ▪ Only limited work has been done on scoping these changes because the shape of the final policy is uncertain. However, the expected timeframe is likely to be in the vicinity of [REDACTED]. If the programme cost is at the higher end of our estimate it is likely to be closer to [REDACTED]. Factors to be considered in determining the appropriate timeframe include: <ul style="list-style-type: none"> ○ The ability to execute the required programme of work for all the systems over the same period of time will be challenging. This work will need to be factored in with all of WNZL’s other projects and divisional priorities work. ○ The complexity involved in scheduling the delivery to achieve timeframes for such a large project. Transitional steps will be required and this adds to the complexity of execution.

	<ul style="list-style-type: none"> ○ Systems will need to interface/connect to a range of other WNZL and WBC systems (both new and existing). This means a significantly increased risk of compatibility issues – both internally and at the customer level. ○ The considerable changes that will be required to WBC domiciled systems (including those supporting Australian customers). [REDACTED] ○ There will be a compound effect on timeframes due to sequencing requirements. Some systems will need to be developed and implemented before others can be commenced. ○ Assuming that some or all of the other banks will be executing similar projects in the same space at the same time, the ability of the New Zealand market to support this will be challenged and could lead to delays. The market is already limited in terms of the legal, technology, payments and project management expertise banks would need to execute projects successfully in areas relating to general ledger, treasury and payments systems and capability. This could hinder banks' ability to comply with their own internal timeframes (and ultimately the regulatory timeframes). ▪ In light of the expected timeframe, it is important to consider that there will be significant developments and changes [REDACTED] by external market and industry changes before they are completed, which will add further complexity and have an effect on timing.
Q21	<p>How much do you think transitioning to compliance will cost and how could those costs be reduced by an appropriate transitional plan?</p> <ul style="list-style-type: none"> ▪ There is currently too much uncertainty with the proposals to provide an estimate of the costs to transition. For example, the Reserve Bank has indicated that it has left open what may constitute "<i>basic banking services</i>" as it wants to obtain the views of stakeholders before making this determination. However, without this information banks do not have a clear idea of what their new compliance requirements will be. ▪ Leaving aside the issue of basic banking services but assuming that the prohibitions on outsourcing to the parent bank are retained, a high level initial estimate of the compliance cost of meeting that requirement is between [REDACTED] ▪ The estimate only covers the system implementation cost and does not include ongoing operational costs of maintaining and supporting new systems and functions. These ongoing costs have been estimated to be [REDACTED] a year. The estimates do not include project costs for managing the overall programme of work or other costs [REDACTED]

ATTACHMENT - MARKET AND BUSINESS IMPACTS

Increased Market, Technology and Operational Risk

- Prohibiting the outsourcing of certain activities to a parent bank runs counter to global system modelling. Most global banking risk models rely on a centralised area of expertise which maintains consistency of approach and model methodology as well as oversight and maintenance of the critical systems, which are then leased out to the regions in which the bank operates. This is accepted by international regulators and the industry generally as good practice. Centralisation has not been raised as a concern by global regulatory bodies or in any Basel edicts.
- If use of centralised systems/expertise hubs were prohibited, this would significantly increase market and operational risk and impact global regulatory reporting, monitoring and compliance requirements. For example, most major banking groups use global liquidity, market and credit risk systems to manage and mitigate risk. If a New Zealand bank was required to operate different or replicated risk systems from the global group, the calculation methodology, underlying data and timing of updates between the group system and the local separately operated system would be different, which could produce different outcomes.
- Decentralised modelling would likely result in:
 - data inconsistencies which would introduce confusion when comparing two different risk results for the same portfolio and unnecessarily increase investigation and resolution times;
 - difficulty for the banking group to understand its global exposures to the different customers, segments and markets;
 - a reduction in the local bank's ability to effectively monitor, report and analyse on risk exposures that are part of the global group exposure; and
 - an increased operational risk environment for the key market, liquidity and credit risk functions.
- Requiring banks to replicate complex global systems and applications within New Zealand would heighten technology and operational risk (including the likelihood of system failures, compatibility issues and resolution times) due to:
 - the need to deploy unproven new systems, applications and interfaces across a highly complex landscape of existing bank systems and functions within a single compliance period;
 - the challenge in connecting a significant number of replicated systems and applications back to a large number of group, third party and parent proprietary systems,
 - the requirement to establish or refresh interfaces with counterparties for payment related transactions; and
 - increased business complexity and disruption from managing and executing a multi-faceted compliance project contemporaneously with planned efficiency and customer focussed initiatives and technology refresh and reliability programmes.

Loss of Global Capability and Efficiency and Customer Impacts

- Most major banks are publicly listed companies in multiple jurisdictions and are required to meet stringent statutory financial reporting and regulatory reporting obligations to a number of different regulators.
- Global banking operations necessitate having a comprehensive and integrated set of financial accounting tools and systems to consolidate financial numbers for a group's total operations, which would be more difficult to achieve if the New Zealand bank's systems were required to be maintained on a standalone basis and were not uniformly and seamlessly connected to the rest of the group.
- For many global functions, including liquidity, market and credit risk and international and financial markets, there is no economic benefit in having systems hosted locally as they require scale to justify the investment, which the New Zealand market does not have. Due to New Zealand's geographic location and market size, gaining access to global suppliers and expertise independent of the parent bank presents a significant challenge.
- Centralisation also provides significant opportunities for the local entity to utilise and benefit from parent bank and global capability in relation to products, operational practice, pricing models, risk management, supply chain management and technology infrastructure.
- If New Zealand banks lose the synergies and benefits of a global banking group's platforms, systems and capabilities, this would:
 - impact centralised global processing and consistency of process for customers;
 - result in a reduction in business efficiency and reliability which currently provides benefits to global customers in terms of product offerings and credit capability and allows for more cost efficient products and services due to economy of scale;
 - limit New Zealand banks' ability to take advantage of diversification benefits existing within portfolios across multiple jurisdictions, which results in lower overall global banking operation risk and therefore improved pricing for customers;
 - result in New Zealand banks not being able to leverage banking group capability (for example for assets, licensing and IP) which would give rise to cost and resourcing inefficiencies;
 - curtail the significant benefits that can be obtained from group led/shared supplier arrangements in terms of cost, scale, negotiation power, access to global supplier '*road tested*' products and associated learnings; and
 - restrict New Zealand banks' ability to be part of a global technology infrastructure planning which enables local banks to adopt current global solutions, use global capability and resources and take advantage of group funded new and refreshed systems.

Project Implementation Challenges and Operational Impacts

- The prohibition on outsourcing certain activities will result in large scale programmes of work affecting a significant number of systems, applications and functions.

- [Redacted]

High Level Estimated Costs²

Prohibited Activity	System Implementation Cost	Operational Costs (per annum)
[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]
TOTALS	[REDACTED]	[REDACTED]

