



APPENDIX A: SUMMARY OF POLICY INTENT DISCUSSIONS

Introduction to Appendix A

This Appendix A records the rationale of the Australian Owned Large Banks (“Banks”) in respect of their proposed changes to the Exposure Draft that appear in Appendix B. All proposed changes relate to a desire to ensure clarity of policy interpretation and consistency of application by the Reserve Bank supervisors and the Banks subject to the policy, or relate to matters of practical workability of the policy. The proposed changes are based on the Banks’ understanding of the Reserve Bank’s policy intent, as discussed at the multilateral workshops between the Large Banks and the Reserve Bank on 27 April, 8 May and 19 May 2017 (“multilateral workshops”).

Appendix A is structured as follows:

- the Banks’ understanding of and/or proposal in relation to each point of clarity discussed with the Reserve Bank is set out under the relevant section heading and section number from the Proposed Exposure Draft in Appendix B, together with the corresponding section heading and section number from the Reserve Bank’s Exposure Draft
- reference is made to the multilateral workshop date and workshop pack page reference of when the matter was last discussed with the Reserve Bank, or otherwise to where a concept or wording is being proposed by the Banks post the last multilateral workshop on 19 May

There are a number of changes in Appendix B that relate to the use of new defined terms, and we have restricted our commentary thereon to the Definitions section rather than on each occasion a new definition is used. There were also a number of instances where the Reserve Bank’s Exposure Draft did not use the defined terms that had been created by the Reserve Bank, so some mark-ups relate to this.

References to the Exposure Draft are to the Reserve Bank’s Exposure Draft of March 2017, and references to the Proposed Exposure Draft are to the Banks’ proposed revised policy document in Appendix B.

Section 1: Introduction
(Section 1 from Exposure Draft)

- This section of the Exposure Draft was not discussed with the Reserve Bank during the multilateral workshops.
- We have moved the policy objectives from paragraph 3.2(1) of the Exposure Draft to paragraph 1.1(2) of the Proposed Exposure Draft as we think that it makes more sense to have the policy objectives clearly stated at the start of the policy (and reflecting the fact that they do not have an operative effect in the policy).
- The change to objective (a) is to capture separation as well as statutory management as we understand that this is the intent.
- The change to objective (b) is to clarify that a change of ownership is intended to relate to where it arises from statutory management or separation, not in the normal course of business.

[\[Page 12 of the 8 May pack\]](#)

Section 2: Definitions and explanations for the policy [Section 2 from Exposure Draft]

Basic Banking Services

- This proposed revised definition largely reflects that discussed at our 19 May multilateral workshop [\[Pages 15 and 16 of the 19 May pack\]](#)
- The preamble has been modified so as to provide clarity that Basic Banking Services is limited to NZD banking services but applies to all customer segments (which enables reference to “customers” throughout the definition rather than “individuals and businesses” as this would risk excluding some entity types including trusts etc)
- We have re-drafted the existing (iv) to create certainty as to what the Reserve Bank considers to be captured by the definition of Basic Banking Services given the need to be able to implement this policy with certainty (including what to plan for and implement over the 5 year transition phase)
- We have included more specific reference to the ability for customers to make payments from and to their transaction accounts (which we assume is the Reserve Bank’s intent)
- We have clarified the word “relevant” to refer instead to the services under 1) to 3) which we assume is the Reserve Bank’s intent
- Part 5) (now part 6)) has been limited to agency banking services as “payments and securities clearing and settlement services” and “correspondent banking” are not customer facing activities – further, settlement services are related to Outcome (a) and correspondent banking is related to foreign currency interbank payments
- Additional changes since 19 May are:
 - “which is deemed” has been changed to “which, for the purposes of this policy” as “deemed” has unintended legal connotations
 - 1) “everyday banking” has been inserted consistent with the wording in the Final Policy Decisions document
 - 1) access to ATMs has been more clearly separated from the ability to make and receive payments
 - 2) has been expanded to reflect the wording in the Final Policy Decisions document
 - 4) credit card merchant acquiring has been reinserted as we understand that the Reserve Bank’s intention is specifically to capture this product, and it doesn’t fit clearly under any of the other items
 - foreign currency term deposits have been added to the list of exclusions included for the avoidance of doubt
 - Bespoke Services have been added to the list of exclusions included for the avoidance of doubt, consistent with the Final Policy Decisions document

Section 2: Definitions and explanations for the policy (continued)

[Section 2 from Exposure Draft]

BCP/DR Capability

- A proposed new definition to capture policy intent regarding Required Risk Mitigants for certain Outsourcing Arrangement Types

Bespoke Services

- A proposed new definition to capture the understood intent in respect of bespoke services not being captured under the definition of Basic Banking Services

Controlled Entity

- A proposed new definition to differentiate Related Parties between controlled and non-controlled entities (“Other Related Parties”), with different resulting Required Risk Mitigants.

[\[Notation E3 on the Policy Scope and Requirements Decision Tree on page 5 of the 27 April pack\]](#)

- Additional changes since 19 May are:
 - Deleted the reference to “but excludes parties that could also be under the control of another party and/ or regulator” and refer instead to the controlled entity being one “that could be subject to an Order in Council under section 117 of the Act” on the basis that this more accurately reflects the wide scope of Reserve Bank statutory management appointment powers.

Critical Functions

- A proposed new definition that captures the functionality underlying Outcomes (a), (b) and (d) of the Exposure Draft [\[pages 6, 8 and 11 of the 19 May pack\]](#)
- Refer to pages 12 to 16 for further explanation including changes since 19 May

Disruption of a Required Outcome Outsourcing Arrangement

- A proposed replacement definition for “Disruption of an outsourcing arrangement” utilised in the proposed new definition “Failure Events”

[\[pages 11 and 12 of the 19 May pack\]](#)

Existing Outsourcing Arrangement

- A proposed new definition used mainly in section 11 (Path to compliance)

Section 2: Definitions and explanations for the policy (continued)

[Section 2 from Exposure Draft]

Failure Event

- A proposed replacement definition for “Day of failure” with similar effect [\[page 5, 8, 9 and 11 of the 19 May pack\]](#)
- Refer to pages 12 to 16 for further explanation including changes since 19 May

Foreign-Owned Banking Group

- A proposed new definition used in paragraphs 4.1, 5.1(3) and 8.1(1)(b) of the Proposed Exposure Draft to allow for the different requirements on non-Foreign-Owned Banks in respect of Robust Back-Up Arrangements and Separation Plans

Fully Automated Basis

- A proposed new definition used in paragraph 5.2(1)(d) of the Proposed Exposure Draft intended to reflect the fact that no system or process is entirely free from person input [\[point 1 on page 13 of the 19 May pack\]](#)

General Procurement

- A proposed new definition used in relation to the definition of Outsourcing to clarify that it is not intended to capture general procurement of services [\[notation A on page 6 of the 27 April pack\]](#)

Implementation Plan

- A proposed new definition related to section 11 of the Proposed Exposure Draft and the Exposure Draft

Independent Third Party

- A proposed new definition intended to clearly refer to third parties that are not Related Parties [\[notation E3 on pages 5 and 7 of the 27 April pack\]](#)

Initial Financial Position Function

- A proposed new definition that captures the functionality underlying Outcome (c) of the Exposure Draft [\[pages 8 and 12 of the 19 May pack\]](#)
- Refer to pages 12 to 16 for further explanation including changes since 19 May

Section 2: Definitions and explanations for the policy (continued)

[Section 2 from Exposure Draft]

In-Progress Arrangement

- A proposed new definition that deals with Outsourcing Arrangements that are being arranged at the time the new BS11 policy Conditions of Registration will first take effect, so as a cut-off can be defined between what is an existing and new Outsourcing Arrangement (and hence when compliance with the new policy is required)

[\[Notation L on page 13 of 27 April pack\]](#)

- This definition has been modified from that included in the 27 April pack, to provide that an Outsourcing Arrangement can be an In-Progress Arrangement if the Bank's internal supplier risk acceptance and approval processes have commenced, and Reserve Bank non-objection has been sought (if applicable). In the 27 April pack, the concept of In-Progress Arrangement required both of these steps to have been completed. We consider this modification to be necessary to reflect the operational reality that in-flight outsourcing arrangements will be relatively advanced, and significant time and resource may have been expended on them, prior to these processes having been finally completed.

List of Pre-Approved Functions and Services

- A proposed new definition in relation to this concept developed by the Reserve Bank in section 6 in the Exposure Draft

Net Liabilities

- Proposed amendment from "banking group" to Related Parties because the definition of Related Parties provides more certainty around which entities are included, as "banking group" is a less clear concept.

Other Related Party

- A proposed new definition to differentiate Related Parties between controlled and non-controlled entities, with different resulting Required Risk Mitigants.

[\[Notation E3 on the Policy Scope and Requirements Decision Tree on page 5 of the 27 April pack\]](#)

Outsourcing Arrangement Provider

- A proposed new definition in relation to the service provider under an Outsourcing Arrangement

Outsourcing

- A proposed amended definition to use other new defined terms and to exclude General Procurement

Section 2: Definitions and explanations for the policy (continued)

[Section 2 from Exposure Draft]

Outsourcing Arrangement Type

- A proposed new definition to clearly distinguish the five types of Outsourcing Arrangement contemplated in the policy, so as to be able to clearly differentiate the Required Risk Mitigants for each Outsourcing Arrangement Type
[\[pages 8 and 10 of 19 May pack\]](#)
- Refer to pages 15 and 18 for further explanation

Parallel Rights

- A proposed amended definition to:
 - use the new defined term “Separation”;
 - capture financial failure as well as Separation; and
 - contemplate contingent contractual arrangements as well as separate contracts

Parent

- A proposed amended definition to clarify that the separation contemplated by the policy is separation from Banks’ overseas bank parents, rather than from any intermediate holding companies in the corporate structure. Such intermediate holding companies will still constitute Related Parties for the purposes of the policy, under limb iii of the definition of Related Party.

Prescribed Contractual Terms

- A proposed new definition that captures the requirements of paragraph 9.1 from the Exposure Draft, so as it can be utilised as a Required Risk Mitigant in paragraph 5.1

Qualifying Change to an Existing Outsourcing Arrangement

- A proposed new definition to define the types of extensions and changes to Existing Outsourcing Arrangements that are not material enough to be considered a new Outsourcing Arrangement, with the implication of the timing of when compliance with the new policy is required

[\[Notation O on page 12 and 13 of the 27 April pack and page 10 of 8 May pack\]](#)

Related Party

- A proposed amended definition to correspond more closely with the more commonly used Companies Act definition, and which we consider will avoid capturing persons that are outside the scope of the control of the Bank and/or its Parent.

Section 2: Definitions and explanations for the policy (continued)

[Section 2 from Exposure Draft]

Required Outcome

- A proposed new definition to define the outcomes in paragraph 4.1 of the Proposed Exposure Draft / paragraph 3.2(2) of the Exposure Draft

[\[page 6 of the 19 May pack\]](#)

- Specifies the intended outcomes as to timing of restoration of capability following the different Failure Events, in relation to the Critical Functions and Initial Financial Position Function
- Refer to pages 12 to 16 for further explanation

Required Outcome Outsourcing Arrangements

- A proposed new definition in relation to Outsourcing Arrangements that are directly relevant to achieving the Required Outcomes

[\[pages 7, 8 and 11 from the 19 May pack\]](#)

- Refer to pages 12 to 16 for further explanation

Required Risk Mitigants

- A proposed new definition to describe the requirements on the banks to have risk mitigants in place in relation to Required Outcome Outsourcing Arrangements, dependent on the Outsourcing Arrangement Type

[\[pages 7 and 8 from the 19 May pack\]](#)

- Refer to pages 17 to 19 for further explanation

Robust Back-Up Arrangement

- A proposed new definition that captures the requirements of paragraph 5.2 from the Proposed Exposure Draft (paragraph 4.1 from the Exposure Draft), so as it can be utilised as a Required Risk Mitigant in paragraph 5.1

Separation or Separates

- A proposed new definition that defines the concept of separation of a Bank from its Parent
- The reference to separation from a Bank's banking group has been removed because we cannot envisage when separation from the banking group, but not from the parent, would occur.

Section 2: Definitions and explanations for the policy (continued)
[Section 2 from Exposure Draft]

Separation Plan

- A proposed new definition simply defining the requirements of a separation plan, for ease of drafting purposes

Thereafter

A proposed amended definition which the banks believe works better from a Reserve Bank perspective from a drafting clarity perspective

Third Party

A proposed new definition simply to create a definition reflecting the Reserve Bank's use of the term "third party", and to clearly distinguish it from the concept of "Independent Third Party" used in the Proposed Exposure Draft

White List

A proposed new definition simply defining the White List contemplated by the Reserve Bank in the Exposure Draft, for ease of drafting purposes

Section 3: Application of the policy
[Section 3 from Exposure Draft]

- It was discussed at the 8 May multilateral workshop that paragraph 3.1(2) in the Exposure Draft was not clear in that it could be interpreted as the policy potentially being applicable to non-Large Banks
[\[Page 11 of the 8 May pack\]](#)
- You confirmed that this was not the intent. You advised that the intent of paragraph 3.1(2) in the Exposure Draft was instead to capture Banks nearing or going below the Large Bank \$10 billion threshold.
- We have proposed wording and a methodology to capture this intended meaning in paragraphs 3.1(1) and 3.1(2) of the Proposed Exposure Draft.
- Paragraph 3.2(1) of the Exposure Draft has been moved to paragraph 1.1(2) as referred to under Section 1: Introduction on page 3.

Section 4: Required Outcomes [Paragraph 3.2(2) from Exposure Draft]

- Paragraph 3.2(2) of the Exposure Draft has been redrafted to reflect the concepts in relation to Required Outcomes discussed at the 19 May multilateral workshop. The drafting closely follows the drafting used in the table on page 8 of the 19 May pack [\[Page 5-9 of 19 May pack\]](#)

The table on page 15 of this Appendix A aims to summarise the core elements of the Outsourcing Policy onto one page to show the link between:

- failure (“Failure Events”);
- outcomes (“Required Outcomes”);
- outsourcing arrangements directly relevant to the outcomes (“Required Outcome Outsource Arrangements”); and
- the policy requirements in relation to such outsource arrangements (“Required Risk Mitigants”)

1

The concept of Failure Events is intended to:

- more clearly show how they drive the Required Outcomes
- enable the Required Outcomes to be differentiated by type of Failure Event, given bank concerns that a Direction given under the Act or a Disruption in relation to a particular Required Outcome could otherwise be seen as requiring all Required Outcomes to be met as if a full financial or operational failure or separation had occurred

2

The proposed Failure Events are drawn from the Reserve Bank’s definition of Day of Failure

- the order has been changed slightly by moving Directions down to event (iii)
- Directions and Disruptions have been limited to those in relation to a Required Outcome

Section 4: Required Outcomes (continued) [Paragraph 3.2(2) from Exposure Draft]

- 3 Required Outcomes have been retained but turned into a defined term and made clearer by splitting them into outcomes related to Initial Financial Position Function (Reserve Bank Outcome (c)) and Critical Functions (Reserve Bank Outcomes (a), (b) and (d)), reflecting the different timing requirements of each, and the fact that the Initial Financial Position Function is only ever required as once-off data on the day of a Failure Event and hence there should not be a requirement for any required back-up arrangement to be sustainable on an on-going and fully automated basis (as there is for Critical Functions). This also reflects the requirements for OBR purposes. Paragraph 4.1(1) bullet point 4 of the Exposure Draft would need to be modified to reflect this, and proposed drafting in this regard appears in the Proposed Exposure Draft at paragraph 5.2(1)(d).
- 4 The separation of the Initial Financial Position Function and Critical Functions definitions re Required Outcomes also makes the drafting easier as it separates the scope of Outsourcing Arrangements requiring a risk mitigant to be in place at all times, from the Required Outcomes (re timings) in relation to such Outsourcing Arrangements following a Failure Event.

The wording of the Critical Functions has the following key proposed changes from the Exposure Draft (recognising that the words re continued provision and timing thereof are dealt with separately in paragraph 4.1 of the Proposed Exposure Draft):

- Reserve Bank Outcome (a) / Critical Function (a) – insertion of the word “interbank” to clarify the reference to settlement obligations vs payment obligations covered under Basic Banking Services [19 May pack], insertion of the word “domestic” to remove international settlements from scope [vs “NZD” in 19 May pack].
- Reserve Bank Outcome (b) / Critical Function (b) – insertion of the word “liquidity” to supplement the risk position requirements [19 May pack], and added reference to prudential supervision reporting and reference to relevant systems and data [outcome of the 19 May multilateral workshop].
- Reserve Bank Outcome (c) / Initial Financial Position Function – removal of “systems” to reflect the one-off nature of this Required Outcome [19 May pack].
- Reserve Bank Outcome (e) – it is proposed that this is moved to the preamble to Outcomes in paragraph 3.2(2) of the Exposure Draft (paragraph 4.1(1) in the Proposed Exposure Draft) as it doesn’t represent a separate Critical Function

Section 4: Required Outcomes (continued)
[Paragraph 3.2(2) from Exposure Draft]

- ⑤ A defined term “Required Outcome Outsource Arrangements” is proposed to define outsource arrangements directly relevant to a Required Outcome, encapsulating the previously discussed definition of “directly relevant”
- ⑥ The Required Risk Mitigants column shows what obligations Banks have under the policy in relation to Required Outcome Outsource Arrangements, depending on the “Outsource Arrangement Type”

Section 4: Required Outcomes (continued)
[Paragraph 3.2(2) from Exposure Draft]

[page 8 of the 19 May pack plus changes discussed (in red) with the Reserve Bank on 19 May]

Failure Events ① ②	Required Outcomes [Items taken from the Outcomes in the Exposure Draft]	Initial Financial Position Function and Critical Functions ③		Relevant Related Outsource Arrangements Requiring Risk Mitigation ⑤	Outsource Arrangement Types ⑥	Required Risk Mitigants ⑥
(i) the Bank is placed into statutory management (ii) a Separation occurs Change to use of defined terms since 19 May workshop	Be able to undertake the Initial Financial Position Function on the day of the Failure Event Be able to undertake the Critical Functions from the start of the Business Day after the day of the Failure Event and Thereafter Change from "Required Outcome" since 19 May workshop	Initial Financial Position Function Critical Functions ④	The collation and reporting of financial data that would be necessary for the New Zealand authorities to have available a range of options for managing the Bank from the start of the first Business Day after the day of the Failure Event and Thereafter [this relates to Outcome (c) of the Exposure Draft] Change from "NZD" since 19 May workshop a. the meeting of a Bank's daily domestic interbank and Reserve Bank settlement obligations (howsoever made now or in the future); [this relates to Outcome (a) of the Exposure Draft] b. the monitoring and management of the Bank's financial position, including credit, liquidity and market risk positions, together with prudential supervision reporting, including the relevant systems and data to do so; and [this relates to Outcome (b) of the Exposure Draft] c. the provision of Basic Banking Services to existing customers of the Bank [this relates to Outcome (d) of the Exposure Draft]	Required Outcome Outsource Arrangements means Outsource Arrangements in relation to a service, function, system, software or application that are directly relevant to a Required Outcome such that without it the Bank would be unable to perform the Required Outcome Added at the 19 May workshop Added at the 19 May workshop	1. Outsourcing Arrangement with an Independent Third Party 2. Outsourcing Arrangement with a Controlled Entity 3. Outsourcing Arrangement with a Controlled Entity who outsources the function to an Independent Third Party 4. Outsourcing Arrangement with an Other Related Party 5. Outsourcing Arrangement with an Other Related Party who outsources the function to an Independent Third Party Words deleted since 19 May workshop following defining of Outsourcing Arrangement	<ul style="list-style-type: none"> Ability to rely on DR and BCP arrangements of the Independent Third Party as determined appropriate by the Bank Requirement for Prescribed Contractual Terms Entry on Compendium <ul style="list-style-type: none"> Ability to rely on DR and BCP arrangements of the Controlled Entity Requirement for Prescribed Contractual Terms Entry on Compendium <ul style="list-style-type: none"> Ability to rely on DR and BCP arrangements of the Independent Third Party as determined appropriate by the Bank Requirement for Prescribed Contractual Terms Entry on Compendium <ul style="list-style-type: none"> Requirement for robust back-up capability Requirement for Prescribed Contractual Terms ** Entry on Compendium Separation Plan <ul style="list-style-type: none"> Requirement for robust back-up capability and / or parallel contractual rights with the Independent Third Party in the event of separation from the Other Related Party Requirement for Prescribed Contractual Terms Entry on Compendium Separation Plan
(iii) a direction is given under the Act in relation to an Initial Financial Position or Critical Function (iv) a Disruption of a Required Outcome Outsourcing Arrangement Correction to relate to defined term used	The Required Outcome relevant to the particular Failure Event		Relevant Initial Financial Position Function or Critical Function	Required Outcome Outsource Arrangements related to the relevant Required Outcome		** = these would likely need to be modified for an Other Related Party re the ability to be provided re regulatory obligations of the Other Related Party

Section 4: Required Outcomes (continued)
[Paragraph 3.2(2) from Exposure Draft]

- The drafting of paragraph 4.1 reflects changes included on page 9 of the 19 May pack.
- As discussed at the 19 May multilateral workshop, wording has been added in respect of the Initial Financial Position Function under Failure Events (iii) and (iv), to reflect the need to continue to maintain the ability to undertake the Initial Financial Position Function post a Failure Event (iii) or (iv) to protect against the risk of a Failure Event (i) or (ii) occurring.

Section 5: Policy scope and risk mitigation requirements [Sections 4 and 9 from Exposure Draft]

Paragraph 5.1

- Section 5.1 of the Proposed Exposure Draft has no direct equivalent in the Exposure Draft. However, it draws together into one place the risk mitigants which are included in various paragraphs in the Exposure Draft (including paragraph 4.1(1), the Guidance Note in section 4, paragraph 9.1, and paragraph 9.2) (requirements for robust back-up capability; requirement for prescribed contractual terms and parallel rights; and BCP/DR requirements for outsourcing to independent third parties), and clearly sets out that the different “Outsourcing Arrangements Types” (outsource to an Independent Third Party, to Controlled Entities etc) and the risk mitigants (“Required Risk Mitigants”) which apply to each.
- Paragraph 5.1 of the Proposed Exposure Draft reflects the right hand two columns of the table summarising the core elements of the Outsourcing Policy discussed at our 19 May multilateral workshop (shown on page 15 of this Appendix A), and, in particular, the table on page 10 of the 19 May pack as shown below on page 18 of this Appendix A.

[\[pages 5 to 8 of the 19 May pack; page 10 of the 19 May pack\]](#)

Section 5: Policy scope and risk mitigation requirements (continued)

[Sections 4 and 9 from Exposure Draft]

- All Required Outcome Outsource Arrangements must have the Required Risk Mitigants in place at all times, in accordance with the requirements for the Outsourcing Arrangement Type deployed, per the following table

Outsourcing Arrangement Type	Outsourcing Arrangement with an Independent Third Party	Outsourcing Arrangement with a Controlled Entity	Outsourcing Arrangement with a Controlled Entity who outsources the function to an Independent Third Party	Outsourcing Arrangement with an Other Related Party	Outsourcing Arrangement with an Other Related Party who outsources the function to an Independent Third Party
Required Risk Mitigants	Ability to rely on DR and BCP arrangements of the Independent Third Party as determined appropriate by the Bank		Ability to rely on DR and BCP arrangements of the Independent Third Party as determined appropriate by the Bank		
		Ability to rely on DR and BCP arrangements of the Controlled Entity			
				Requirement for robust back-up capability	Requirement for robust back-up capability and /or parallel contractual rights with the Independent Third Party in the event of separation from the Other Related Party
	Requirement for Prescribed Contractual Terms	Requirement for Prescribed Contractual Terms	Requirement for Prescribed Contractual Terms	Requirement for Prescribed Contractual Terms **	Requirement for Prescribed Contractual Terms
	Entry on Compendium	Entry on Compendium	Entry on Compendium	Entry on Compendium	Entry on Compendium
				Separation Plan	Separation Plan

** = these would likely need to be modified for an Other Related Party re the ability to be provided re regulatory obligations of the Other Related Party

Section 5: Policy scope and risk mitigation requirements (continued)
[Sections 4 and 9 from Exposure Draft]

Paragraph 5.2

- Paragraph 5.2 of the Proposed Exposure Draft largely incorporates the robust back-up arrangement requirements included in paragraph 4.1 of the Exposure Draft.
- Paragraph 5.2(1)(d) of the Proposed Exposure Draft (paragraph 4.1(1) bullet point 4 of the Exposure Draft) has been changed to reflect the discussion during the 19 May multilateral workshop. On the basis of this discussion, we understand that the Reserve Bank recognises that it is possible that an Outsource Arrangement could be directly related to a Required Outcome, and yet not need to be provided on an ongoing basis post a Failure Event. For example, a Bank might have a separate outsourced system which it uses to determine risk positions in respect of a product that does not fall within Basic Banking Services. In this example, a Bank must have a Robust Back-Up Arrangement for the relevant system, to enable it to monitor its risk positions immediately following the Failure Event, and for the period until all relevant positions have been run off. However the Robust Back-Up Arrangement does not need to be equally substitutable for the Outsourced Arrangement, and capable of operating on an ongoing, fully automated basis. Rather, a Bank will only need to demonstrate that it can switch to a Robust Back-Up Arrangement which is appropriately robust in the circumstances, in this instance until the product could be expected to be fully run off.

[\[page 13 of the 19 May pack\]](#)

- Additional changes since 19 May are:
 - the change to paragraph 5.2(1)(a) of the Proposed Exposure Draft (paragraph 4.1(1) bullet point 1 of the Exposure Draft), is intended to provide greater clarity in respect of the relevant requirement, so as to provide greater certainty for Banks and external reviewers as to whether the requirement is being met.
 - the change to paragraph 5.2(1)(b) of the Proposed Exposure Draft (paragraph 4.1(1) bullet point 2 of the Exposure Draft) in relation to compliance with conditions of registration in relation to Open Bank Resolution (OBR) have been removed as in the banks' view this is not required to be repeated in the Outsourcing Policy.
 - changes to paragraph 5.2(1)(e) of the Proposed Exposure Draft (paragraph 4.1(1) bullet point 5 of the Exposure Draft) which we consider are necessary to clarify the scope of the testing requirements and make them operationally workable.
 - paragraph 4.1(1) bullet point 6 does not appear in the Proposed Exposure Draft as this is already addressed in Sections 11 and 12.

Section 5: Policy scope and risk mitigation requirements (continued)
[Section 4 and 9 from Exposure Draft]

Paragraph 5.3

- We understand that the concept of Alternative Arrangements was introduced by the Reserve Bank to allow the Banks to come up with innovative solutions to achieve the policy objectives on a cost effective basis where possible and required
- Outsourcing Arrangements that are clearly with entities under the control of the Bank (and can't be frustrated by an overseas authority) have been proposed to be separated out as "Controlled Entities", with associated Outsource Arrangement Types (refer the table on page 18) and Required Risk Mitigants
- We have proposed that the concept of Alternative Arrangements remain but is modified to deal with Alternative Arrangements where the Bank does not have control of the entity it is outsourcing to, but the arrangement is still not able to be frustrated by a related party or overseas prudential regulatory authority
- Such arrangements would need to be approved by the Reserve Bank on a case-by-case basis as contemplated in paragraph 4.3 of the Exposure Draft
[\[page 22 of the 8 May pack\]](#)

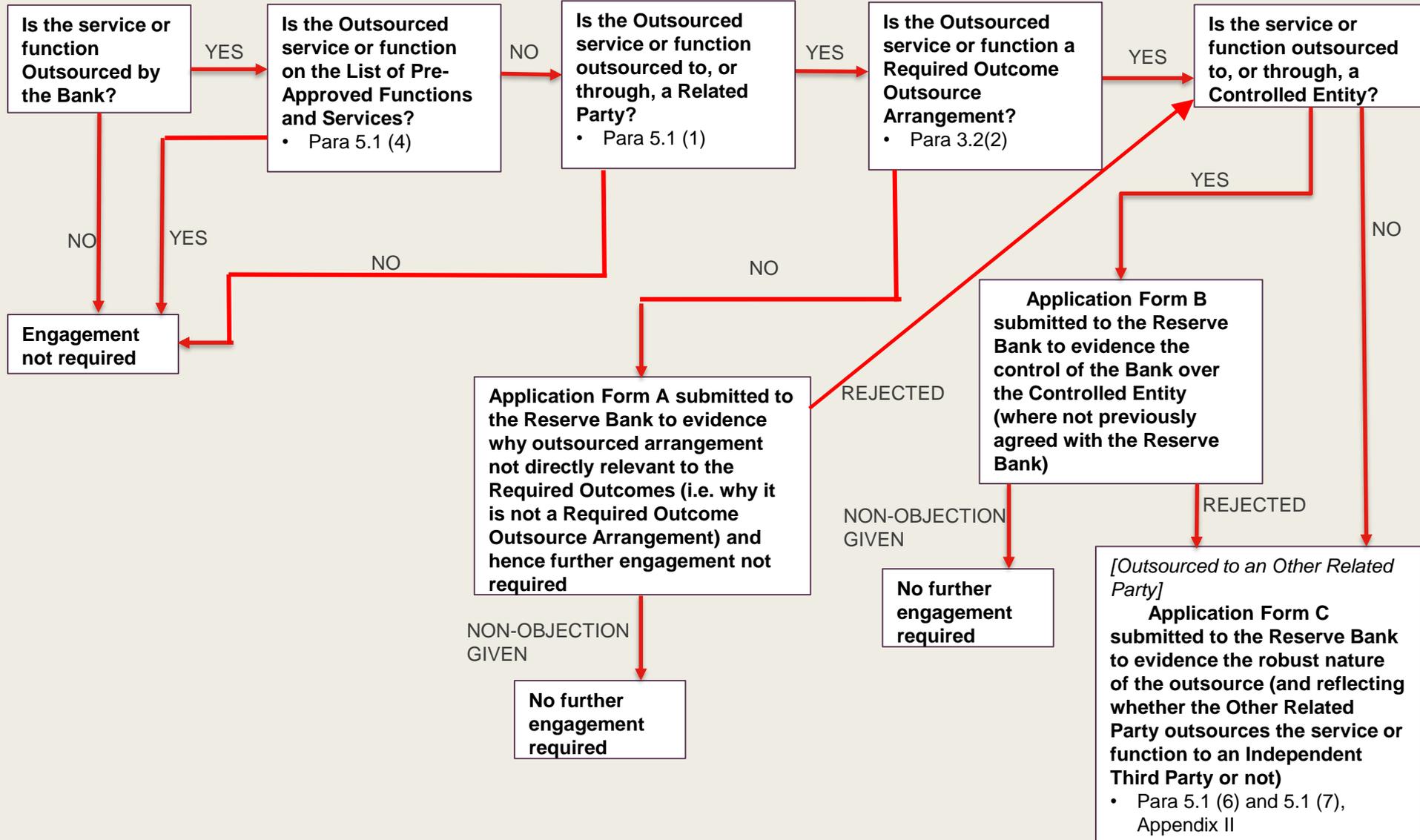
Section 6: Engagement Process [Section 5 from Exposure Draft]

- This section was discussed with the Reserve Bank at the 27 April multilateral workshop [\[pages 8-9 of the 27 April pack\]](#) and again at the 8 May multilateral workshop [\[page 26 of the 8 May pack\]](#). The Decision Trees presented at those meetings has changed slightly to reflect our understanding of the Reserve Bank's intent – i.e. that engagement is not required in respect of outsourcing to Independent Third Parties or in relation to Outsourcing on the List of Pre-Approved Functions and Services, such that only Outsourcing Arrangements with Related Parties require engagement in respect of Application Forms A, B and C [\[new Engagement Process Decision Tree on page 23\]](#)
- The changes made to this section of the Exposure Draft are designed to drive certainty for Banks, while also providing the Reserve Bank visibility on proposed Outsourcing Arrangements – both where a Bank considers they are relevant to the Required Outcomes, and where a Bank considers they are not.
- To this effect, we have adapted Appendix II from the Exposure Draft to now form Appendices II, III and IV, which make up Application Forms A, B and C. As discussed at the 27 April multilateral workshop, these application forms are designed to front-end engagement between the Reserve Bank and the applicant Bank to ensure the Reserve Bank has the necessary information to come to a view as to whether it will provide non-objection or not.
- The three application forms serve three different purposes:
 - Application Form A would be used where an Outsourcing Arrangement is not on the White List, but a Bank considers that it is not directly relevant to a Required Outcome. In order to avoid the possibility of a “back-door” materiality threshold, we are proposing that Banks would submit a form outlining the relevance (or lack thereof) of the Outsourcing Arrangement to the Reserve Bank and seeking non-objection to that view. For this reason, Application Form A steps out the impact a disruption would have on the Bank's ability to meet any Required Outcome. Where the Reserve Bank agrees with the Bank's assessment that an Outsourcing Arrangement is not directly relevant to any Required Outcome, this could then proceed to a consultation discussion with all Large Banks on whether this item (or a generalised category thereof) should be added to the White List.
 - Application Form B would be used where an Outsourcing Arrangement is with a Controlled Entity. In this case, the applicant Bank is required to demonstrate to the Reserve Bank that the entity is under the control of the Bank and is able to be placed in statutory management under the Reserve Bank Act. Where a Bank has demonstrated that it controls an entity, we envisage that this entity would go on the Pre-Approved List for that bank, assuming no change of control of the Controlled Entity occurs.

Section 6: Engagement Process (continued)
[Section 5 from Exposure Draft]

- Application Form C is an expansion of the existing Appendix II of the Exposure Draft. This also outlines the impact of a disruption on the Bank's ability to meet any Required Outcome, and goes on to identify why the Bank considers the back-up arrangement to be robust. This is achieved by spelling out how the Required Outcome Outsourcing Arrangement meets the requisite aspects of paragraph 5.2 of the Proposed Exposure Draft (Robust Back-Up Arrangements for functions Outsourced to an Other Related Party). We are proposing to delete paragraphs 5.1(6) and (7) of the Exposure Draft, and instead, incorporate these considerations into Application Form C by requiring the applicant Bank to confirm it has completed supplier risk analysis and due diligence. This will ensure that the applicant Bank addresses the relevant considerations before making its application.
- As in the Exposure Draft, the Reserve Bank can request clarification information if it considers that the information in any application form is insufficient to enable it to provide non-objection. On this basis, we propose to delete paragraph 5.1(11) of the Exposure Draft, as the three application forms will require the applicant Bank to provide all the information that is relevant for the purposes of the particular type of application. We understand that therefore, additional information requests would generally only occur if an applicant Bank has not provided adequate information in respect of an aspect in the relevant application form.
- We are also proposing to delete the Guidance Note regarding the options available to the Reserve Bank upon receipt of an application, and incorporate these options into the new paragraphs 6.1(4), (5) and (6). This approach will provide greater clarity for applicant Banks and the Reserve Bank in setting out the application and consideration processes.
- We also propose to delete 5.1(9) of the Exposure Draft, and incorporate a "time freeze" in new paragraphs 6.1(4), (5) and (6) for the period the Bank takes to provide any requested additional information to the Reserve Bank. We consider this is necessary to provide certainty for Banks on the timing of the application process.
- We have not proposed a tightening of the response times on any application, and appreciate the comment at the 27 April multilateral workshop that these will continue to be addressed on a "best endeavours" basis within the 20 working days, with our experience to date being that these are turned around quickly.

Section 6: Engagement Process (continued)
[Section 5 from Exposure Draft]



Section 7: Compendium
[Section 8 from Exposure Draft]

- In paragraph 7.1(1) of the Proposed Exposure Draft (paragraph 8.1(1) of the Exposure Draft) we have deleted the words “as some outsourcing arrangements may relate to time critical obligations”, on the basis that all information in the Compendium needs to be readily available irrespective of whether the outsourced service or function is time critical or not.
- In paragraph 7.2(1) of the Proposed Exposure Draft we have deleted what was 8.2(1)(b) of the Exposure Draft on the basis that the information on costs is commercially sensitive and is not relevant to the Reserve Bank or a statutory manager.
- In paragraph 7.5(1) of the Proposed Exposure Draft (paragraph 8.5(2) of the Exposure Draft) we have changed the reference to an external auditor to an external reviewer so as we can leverage the existence and knowledge of the external reviewer contemplated in sections 11 and 12 of the Exposure Draft.
- In paragraph 7.6(1) of the Proposed Exposure Draft (paragraph 8.6(1) of the Exposure Draft) we have made changes to reflect that Banks endeavour to operate on a paperless basis. However, we have provided for printed extracts of information in the Compendium to be made available to the Reserve Bank if required.

Section 8: Separation Plan **[Section 10 from Exposure Draft]**

Paragraph 8.2

- Paragraph 8.2(1) of the Proposed Exposure Draft includes amendments to reflect the discussion during the 27 April multilateral workshop, to clarify that the Separation Plan is only required to address outsourcing arrangements which are directly relevant to the policy outcomes i.e. Required Outcome Outsource Arrangements.

[\[Notation R on page 11 of the 27 April pack\]](#)

Paragraph 8.2

- Amendments to paragraph 8.2(2) of the Proposed Exposure Draft (second paragraph in section 10.2(1) of the Exposure Draft), and the proposed new Guidance Notes below sections 8.2(2) and 8.2(3) of the Proposed Exposure Draft, are included to clarify the scope of the Separation Plan, as discussed at the 19 May multilateral workshop. In particular, they clarify that the Separation Plan is required to show how the Bank will meet the Required Outcomes after Separation (rather than continuing to operate on a “business as usual basis”), and that this applies only in respect of services or functions directly relevant to the Required Outcomes that were previously outsourced to a Related Party. Consistent with that, the specific items which were listed in paragraphs 10.2(1)(a) –(g) of the Exposure Draft have been deleted, and replaced with a reference to the Required Outcomes.

[\[Item 4 on page 13 of the 19 May pack\]](#)

- Paragraph 8.2(5) of the Proposed Exposure Draft (paragraph 10.2(4) of the Exposure Draft) includes a requirement for the Reserve Bank to consult with the Banks before issuing guidance on the content of Separation Plans. This was not discussed during the multilateral workshops, but the Banks consider that a requirement to consult is appropriate in this instance, as the nature of the guidance may have substantive practical implications for Banks.

Section 8: Separation Plan (continued)
[Section 10 from Exposure Draft]

Paragraph 8.3

- Paragraph 8.3(2) of the Proposed Exposure Draft has been added to reflect the discussion at the 19 May multilateral workshop, that development of the Separation Plan will be an iterative process, tied to a Bank's path to compliance.
- Paragraph 8.3(7) of the Proposed Exposure Draft (paragraph 10.3(5) of the Exposure Draft) reflects the discussion at the 27 April multilateral workshop, so that minor, administrative changes to a Separation Plan do not need to be reported to the Reserve Bank.

[\[Notation T on page 11 of the 27 April pack\]](#)

Paragraph 8.4

- As discussed at the 27 April multilateral workshop, paragraph 8.4(2) of the Proposed Exposure Draft (paragraph 10.4(2) of the Exposure Draft) has been amended to reflect that, due to timing of board meetings, it may not be possible to always report Separation Plan test results within four weeks of completion.

[\[Notation U on page 11 of the 27 April pack\]](#)

- Paragraph 8.4(3) of the Proposed Exposure Draft (paragraph 10.4(3) of the Exposure Draft) has been amended to provide greater certainty on when impediments must be notified to the Reserve Bank, and the nature of the notification that will be required. This reflects the discussion at the 27 April multilateral workshop.

[\[Notation S on page 11 of the 27 April pack\]](#)

Section 9: Maintenance of List of Pre-Approved Functions and Services [Section 6 from Exposure Draft]

- Having defined List of Pre-Approved Functions and Services in Section 2 of the Proposed Exposure Draft, and addressed engagement on pre-approved items in section 6 of the Proposed Exposure Draft, section 9 of the Proposed Exposure Draft (section 6 of the Exposure Draft) is now purely related to the maintenance of the list.
- We propose to remove the Guidance Note, and include the process by which a Bank can apply to have a function or service added to the List of Pre-Approved Functions and Services in paragraph 9.2 of the Proposed Exposure Draft. This will provide greater clarity for the Reserve Bank and the Banks.
- We have also included a requirement for the Reserve Bank to consult with the Banks before making a decision on an application for a function or service to be added. This will ensure that when the function or service is added, the Reserve Bank and the Banks share the same understanding as to what that definition is intended to capture. From our discussions at the multilateral workshops, we understand this to be the Reserve Bank's intention in relation to the maintenance of the List of Pre-Approved Functions and Services.

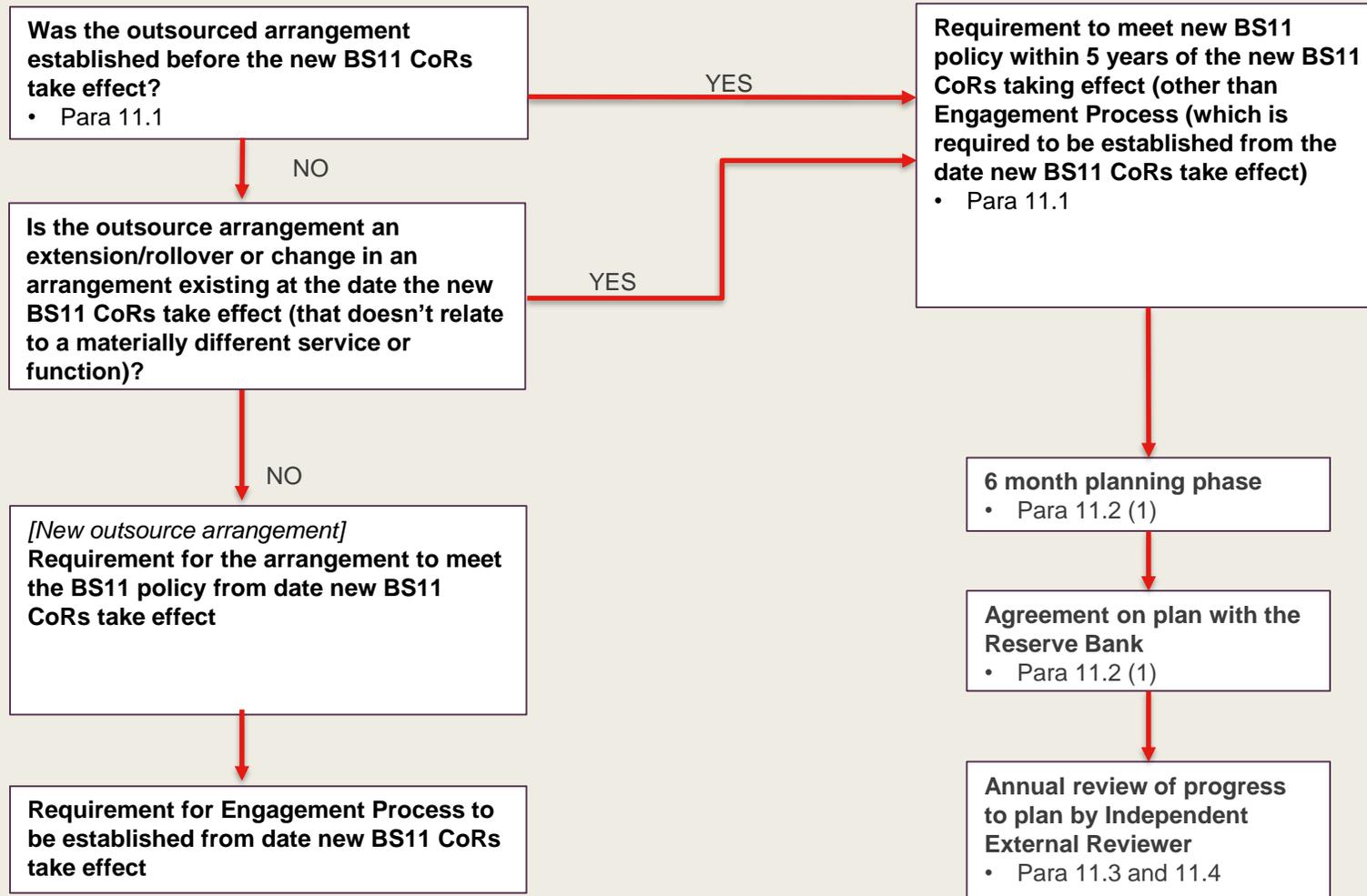
Section 10: Maintenance of the White List
[Section 7 from Exposure Draft]

- We propose to amend paragraph 7.1(1) in the Exposure Draft, and incorporate this content into the definition of "White List".
- We propose to remove the Guidance Note under paragraph 7.1(1) in the Exposure Draft, and include the process by which a Bank can apply to have a function or service added to the White List in the new paragraph 10.2 of the Proposed Exposure Draft. This will provide greater clarity for the Reserve Bank and the Banks.
- We also propose to include a requirement for the Reserve Bank to consult with the Banks before making a decision on an application for a function or service to be added. This will ensure that when the function or service is added, the Reserve Bank and the Banks share the same understanding as to what that definition is intended to capture. From our discussions at the multilateral workshops, we understand this is to be the Reserve Bank's intention in relation to the maintenance of the White List.
- We have suggested a process to agree a path to compliance between the Reserve Bank and impacted Large Banks where an item is taken off the White List. This is to ensure that where an item is removed, Banks have an opportunity to transition this service or function to become compliant with BS11 and remove the risk of Banks becoming non-compliant immediately following a change to the White List.

Section 11: Path to compliance and external review **[Section 11 from Exposure Draft]**

- We have added a new paragraph 11.1(1) in the Proposed Exposure Draft to explain when a Bank is required to have an Implementation Plan.
- A new paragraph 11.2(1) in the Proposed Exposure Draft has also been added to make it clear that the engagement process applies immediately the new BS11 Conditions of Registration of a Bank first take effect.
[\[Notation M on page 13 of the 27 April pack\]](#)
- A new paragraph 11.3 in the Proposed Exposure Draft makes it clear that new Outsourcing Arrangements entered into after the new BS11 Conditions of Registration first take effect must comply with the requirements of the revised BS11 policy from their inception, other than In-Progress Arrangements [\[Notation L on page 13 of the 27 April pack\]](#) and Qualifying Changes to an Existing Outsourcing Arrangement [\[Notation O on page 10 of the 8 May pack\]](#).
- Paragraph 11.4(2) of the Proposed Exposure Draft replaces paragraph 11.2(1) and the accompanying Guidance Note in the Exposure Draft. It allows a Bank to have six months to prepare an Implementation Plan and for the Reserve Bank to have an additional three months to agree to it. Further, paragraph 11.4(2) in the Proposed Exposure Draft sets out the information a Bank needs to provide to obtain the Reserve Bank's approval to the Implementation Plan [\[Notation P on page 14 of the 27 April pack\]](#). Items (b) and (c) of this list have now been limited to Robust Back-Up Arrangements in the Proposed Exposure Draft.
- Paragraph 11.4(4) of the Proposed Exposure Draft (paragraph 11.4(2) of the Exposure Draft) provides for the terms of reference for external reviewers to be consistent across all banks.
[\[Path to Compliance Decision Tree on page 30\]](#)

Section 11: Path to compliance and external review (continued)
[Section 11 from Exposure Draft]



Section 12: Three-yearly external review following the transition path to compliance
[Section 12 from Exposure Draft]

- This section of the Exposure Draft was not discussed with the Reserve Bank during the multilateral workshops.
- The changes to this section are not substantive and are made purely for consistency purposes and to utilise the new defined terms.

Appendix I: Conditions of Registration [Appendix I from Exposure Draft]

We consider that Condition of Registration (1) should be redrafted. We consider that the current reference in Condition of Registration (1) to the “legal and practical ability to comply” with the policy as a whole is confusing and should be reconsidered.

More generally, we consider that the Conditions of Registration should be revised to more specifically set-out the relevant compliance requirements.

We consider that this approach is necessary to deal with the complexities of the transitional period for the policy, and, in particular, to reflect that different requirements will apply in respect of new and existing outsourcing arrangements, while banks will also need to separately demonstrate they are meeting the path to compliance requirements. In our view, a more specific and tailored Condition is therefore necessary to provide certainty for management and board attestations during the transitional period.

Consistent with the above, we have not proposed revised wording for Condition of Registration (1), because we consider that the precise wording of the Condition will require careful consideration once the content of the final policy has been settled. We would welcome the opportunity to engage further with the Reserve Bank on the content of the Condition, and note that, for the reasons given above, we consider that a longer period than 7 days may be required to allow banks a reasonable opportunity to consider and make submissions on the Condition.