September 24th, 2018

**GENERAL COMMENTS ON THE EBA CONSULTATION ON DRAFT GUIDELINES ON OUTSOURCING**

The Spanish Banking Association (AEB) welcomes the opportunity to make comments to the EBA Consultation on draft Guidelines on outsourcing.

As members of the European Banking Federation (EBF), we have contributed to the drafting of its response and therefore, we support the main issues identified by the whole European banking industry.

Although we consider these guidelines to be a positive step towards achieving regulatory harmonisation by taking definitions and requirements already included in other EU financial regulations, we are concerned about the impact that the proposed guidelines could have on the competitive position, cost structure and innovation potential of financial institutions.

For that reason, we would like to take the opportunity to contribute to the public debate to highlight the main concerns of our banks.

**Facilitating banks’ digital transformation and competitiveness**

Financial Institutions offer a wide range of products and services and not all of them require a license. Consequently, financial institutions compete with a wide diversity of firms in activities such as payments, lending or financial advice. Those firms can have different legal forms, capital requirements or oversight controls, among others. Also, non-European affiliates of European entities need to be able to compete on an equal footing in their local markets.

Therefore, it is important ensuring that the application of these Guidelines does not hinder the ability of financial institutions to compete both with those usually more flexible and less regulated firms offering banking services and products in EU as well as with non-EU financial institutions in their local markets.

**Outsourcing definition and criticality criteria**

The definition of outsourcing is not clear and leaves room for interpretation. Besides, it is very broad (in particular, words such as “any arrangements”) and it could be interpreted as including all third-party arrangements.

Although we positively value the EBA’s approach to harmonize outsourcing definitions among different regulations, the application of these Guidelines should not increase substantially the number of third-party arrangements considered outsourcing. On the contrary, this could increase the compliance burden, the regulatory costs and the competitive position of financial institutions.

Therefore, activities not requiring a banking license should be out of the scope of these Guidelines. Moreover, they should clearly differentiate the requirements for the outsourcing of critical and non-critical functions, providing lighter requirements for those considered non-critical. At the same time, the provided list of examples of arrangements not considered outsourcing should be clearly stated as non-exhaustive. In addition, it would be very positive if a more detailed list was provided. This would avoid that non-licensed companies offering non-exclusive financial services are given a competitive advantage before regulated financial institutions.

**Sub-outsourcing**

Sub-outsourcing assessment is one of the critical issues for the risk assessment, due diligence and oversight of outsourcing providers. Institutions find difficult to perform the risk assessment and monitoring of sub-outsourcing activities through the whole outsourcing chain, which potentially might be long. In addition, it will not only depend on suppliers to inform about changes in their supply chain –information that has commercial value and that not all service providers may always be willing to provide - but also on institutions being able to access and perform the due diligence of sub-service providers.

The monitoring of sub-outsourcing chain by the financial institution will not be feasible in many cases. For this reason, we believe that the financial entity should only be responsible for the direct relationship with its provider. Further responsibility to ensure that the sub-outsourcing complies with the agreed terms should lie within the company that decides to sub-outsource.

**Access’ rights**

Unrestricted access rightmight become very problematic and difficult to apply in practice, since it is subject to the supplier’s willingness to allow this clause in their agreements. We believe this should only be required in case of outsourcing of critical functions.

**Notification process**

This requirement is currently subject to diverging interpretations of National Competent Authorities and already affects the time-to-market of new initiatives in those countries such as Spain, where this requirement could be understood as a kind of authorization process. To avoid this fragmentation and any potential impact on the competitive position of some institutions, this requirement should be removed or at least converted in an ex-post notification, as it already happens in other member states such as France. Beyond pure notifications, the ongoing dialogue between entities and authorities within the supervision context will also facilitate that authorities have sight on the entities’ future plans and that the processes are transparent.

**Technology neutrality**

Outsourcing activities to cloud service providers is treated as a special case by the proposed guidelines, which classifies as outsourcing any service supported by cloud technologies. We believe this could disincentivize the use of cloud computing, a technology that offers cost, resiliency and flexibility advantages and is widely used by innovative companies, some of them already offering financial services. We propose instead these guidelines to follow a technology neutral approach and base the consideration on the nature of the outsourced functions and not on the technology used.

**Intragroup outsourcing**

Intragroup outsourcing seems to be considered by the Guidelines as an especially risky case of outsourcing. However, we believe that outsourcing to a limited set of group service providers can be very beneficial as long as it is implemented in a controlled and systematic way.

At intragroup level, there is a range of facts that facilitate risk control. Specifically, our banks have mechanisms for the control of vendors in all entities and of the intra-group companies that guarantee at a Group level that the oversight and control of all activities is coherent.

In addition, these Guidelines overestimate the risks posed by intra-group outsourcing by disregarding the higher ability of institutions to control companies within their consolidation perimeter and the complementary measures and controls already required by other financial regulations such as the Bank Resolution and Recovery Directive.

For all of that, we think that intragroup outsourcing should be subject to lower compliance and reporting obligations than third-party outsourcing agreements.

Furthermore, the application of these Guidelines should not create a competitive disadvantage for those Groups with subsidiaries outside the EU in comparison with other local competitors not subject to these rules.

**Audit function**

The proposed guidelines seem to be pointing exclusively to the audit function for the monitoring of outsourcing. However, we believe that the coverage of outsourced activities reviews, including on-site visits, performed under audit rights enforcements, should be set at an institution level and should be performed, under a risk-based approach plan, either by the second line of defense, specialized functions or a combination of all these.

**Recovery and resolution**

EBA guidelines need to be consistent with the recovery plans while at the same time ensuring resolvability. It is essential that the recovery plans and all the actions and policies designed by entities should be integrated into the supervisory assessment of compliance with the Guidelines so that firms are not required to unnecessarily duplicate (or unintentionally contradict) the work that have gone in designing theses plans.

**Involvement of management body**.

The involvement of management body should be kept high-level. Therefore, management body should only be required to participate in the definition and approval of the high-level outsourcing policy and in the reporting of material risks.

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Lastly, we would like to stress that Controls required by the proposed framework on suppliers are very demanding, sometimes even impossible to ensure on an individual basis for financial institutions.

We believe authorities should acknowledge this fact and support the financial industry efforts, so they can better ensure that concentration risk (on very few providers) is properly monitored and managed.

In our view, the following measures could facilitate this process:

* Authorities direct control on service providers. This would be very efficient, for both financial institutions and providers, as there would only need to be one verification instead of a repeated exercise by all the individual entities. There are already some precedents in certain infrastructures and services that are used by all the industry, such as CCPs or benchmarks, for which a process of authorization is in place whereby supervisors monitor their soundness and integrity. We would suggest this measure to be used when outsourcing services are concentrated in one or a few dominant service providers in the financial sector which could become a single point of failure for the whole financial system. The direct monitoring by authorities would ensure that specific worries noted by them, such as concentration risk, are properly monitored and managed. At the same time, authorities would naturally have more power to supervise them than individual entities, given the reduced bargaining power.
* In complement to this, the EBA could also explore the possibility to promote certification schemes for providers, in line with the works of the European Commission Working Group on Cloud security certification schemes, which are specifically applicable to the financial sector. This would also increase the efficiency of the process, avoiding each bank to repeat the assessment of the same provider.
* Authorities could also support the industry efforts by providing a check-list of the requirements needed by financial institutions, so that outsourcing providers could have a clear list and get ready for them. There is a positive precedent on the EBA recommendations to cloud outsourcing, which facilitated the dialogue with providers and their understanding of the need to include certain elements in the contracts.