



Securities Industry Association

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October 20, 2004

Philippe Richard
IOSCO Secretary General
Oquendo 12
28006 Madrid
Spain

Re: Principles on Outsourcing of Financial Services for Market Intermediaries.

Dear Mr. Richard:

The Outsourcing Subcommittee of the Technology & Regulation Committee of the Securities Industry Association¹ appreciates the opportunity to provide comments on the above-referenced IOSCO Consultation Report. The Consultation Report sets out a set of principles that are designed to assist regulated entities in determining the steps they should take when considering outsourcing activities. We understand that comments were requested by September and so we very much appreciate your willingness to consider our comments on this important effort.

SIA commends the IOSCO Technical Standing Committee on Market Intermediaries for its work in developing these principles. SIA offers the following comments on the draft principles that we hope will be considered in the course of the consultation process that leads to publication of a final report.

¹ ¹The Securities Industry Association, established in 1972 through the merger of the Association of Stock Exchange Firms and the Investment Banker's Association, brings together the shared interests of nearly 600 securities firms to accomplish common goals. SIA member-firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs 790,600 individuals. Industry personnel manage the accounts of nearly 93-million investors directly and indirectly through corporate, thrift, and pension plans. In 2003, the industry generated \$213 billion in domestic revenue and an estimated \$283 billion in global revenues. (More information about SIA is available on its home page: www.sia.com.)

1. Definition of outsourcing.

(a) We believe that the term “outsourcing” should be limited to the transfer of functions to a service provider that directly impact the outsourcing firm’s operational risks or ability to meet its regulatory requirements or service its clients. The current definition covers topics as diverse as cafeteria services and travel services, which are tangential to the firms’ client business.

(b) The Report also should clarify that the term “outsourcing” refers to the transfer from a regulated firm to a service provider of a function where management of the particular function is transferred with the function.² The term outsourcing need not include engagements where the firm retains day to day management responsibility for the function, such as in supplemental resourcing arrangements, where contract consultants act as additional resources on teams led and managed by the firm. In such examples, the firm does not transfer management of the function to the contractors or the service provider. If the firm retains management of the function, the risks to the firm do not change materially, regardless of whether the particular resources consist of individual employees or contractors. Therefore there is no need for application of additional risk management guidelines proposed in the Report.

2. Protection of confidential customer information. The Report provides that firms “are expected to take appropriate steps to confirm that confidential customer information is not misused or misappropriated.” Regulated outsourcing firms have to comply with and ensure that their service providers comply with applicable laws protecting against the inappropriate disclosure of customer information. The Report also provides, however, that regulated entities should consider “whether it is appropriate to notify customers that customer data may be transmitted to a service provider.” If this language suggests additional requirements beyond what is required by the laws and regulations of the regulated firm’s own jurisdiction and beyond any applicable contractual requirement imposed by the laws and regulations of foreign jurisdictions, then the Report may be imposing requirements that other legislators and regulators have decided not to adopt. We believe this is unnecessary.³

3. Service provider compliance with law. The Report requires that the outsourcing firm implement “processes and procedures designed to help ensure that the service provider is in compliance with applicable laws and regulatory requirements in its jurisdiction, and that where there is a failure to perform duties required by statute or regulations, the outsourcing firm, to the extent required by law or regulation, reports the failure to its regulator and/or SRO and takes corrective actions.” (See p.6.) This could

² The Report currently defines outsourcing as “an event in which a regulated outsourcing firm contracts with a service provider for the performance of any aspect of the outsourcing firm’s regulated or unregulated functions that could otherwise be undertaken by the entity itself.” (See p.1.)

³ As the Report states, “Regulators should seek to become aware of whether outsourcing firms within their jurisdictions are taking appropriate steps to monitor their relationships with service providers with respect to the protection of confidential customer information.” (See p.11.)

suggest that an outsourcing firm is responsible for identifying where a service provider is not in compliance with laws and regulatory requirements in the service provider's own jurisdiction, even for activities not associated with the outsourcing firm. We suggest rewording to clarify that, to the extent required by law or regulation and to the extent an outsourcing firm becomes aware of the violation, the duty to report is limited to violations of laws and regulatory requirements by the service provider that relate to services performed for or on behalf of the outsourcing firm.

4. Outsourcing to affiliates. Clarification is needed on the comment that the Outsourcing Principles must be applied to affiliated entities, albeit with some modification as appropriate.

Focus for affiliates should be on the firm's global policies and management controls. The goal is to ensure that appropriate attention is paid to the potential risks associated with outsourcing. Firms that have global policies in areas such as (i) business continuity (inclusive of exit strategies for business interruptions), (ii) confidentiality, (iii) information security and (iv) physical security, to name a few, have addressed these risks by issuing and enforcing these policies within the firm on a global basis. Similarly, where the service requirements between affiliates are adequately established and managed, effective corporate governance will ensure that these service levels are enforceable. Extending the formality of a written contract adds no value in such instances.

SIA appreciates the opportunity to comment on the Consultation Report and would be happy to address any questions you may have concerning our views. Please address questions to the undersigned or to Scott Kursman, Vice President & Associate General Counsel, SIA, at 212-618-0508.

Very Truly Yours,

Scott Kursman
Vice President &
Associate General Counsel

cc: Ms. Randee Pavalow, Director, Capital Markets,
Ontario Securities Commission