



Utkarsh Small Finance Bank

POLICY FOR OUTSOURCING OF FINANCIAL AND IT SERVICES

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Contents

1. BACKGROUND	4
2. DEFINITION	4
3. APPLICABILITY	4
4. ACTIVITIES THAT CANNOT BE OUTSOURCED	5
5. COMMON AREAS OF OUTSOURCING	5
a) Banking Operations	5
b) Technology Operations	6
6. FRAMEWORK FOR APPROVAL	6
7. ROLE AND RESPONSIBILITY OF OUTSOURCING COMMITTEE	7
7.1 Regulatory and Supervisory requirements	7
7.2 Due diligence measures to be adopted	8
7.3 Due diligence of service provider.....	8
8. OUTSOURCING AGREEMENT.....	9
8.1 Termination clause	10
8.2 Sub-Contracting	10
8.3 Dispute resolution	10
8.4 Applicable laws	11
9 OUTSOURCING OFF-SHORE AND WITHIN A GROUP.....	11
9.1 Off-shore Outsourcing of financial services (Outsourcing to Foreign Service providers)...	11
9.2 Outsourcing within a group	12
10 CONTROL ENVIRONMENTS OFFERED BY THE SERVICE PROVIDER.....	12
10.1 Confidentiality and security	12
10.2 Responsibilities of DSA/DMA/ recovery agents.....	13
11. MONITORING AND CONTROL OF OUTSOURCED ACTIVITIES.....	13
11.1 Structure for management and control of Outsourcing.....	13
11.2 Service level agreements and performance metrics	13
11.3 Measuring by key performance indicators (KPIs)	14
12. BUSINESS CONTINUITY AND MANAGEMENT OF DISASTER RECOVERY PLAN	14
13 GRIEVANCES RELATING TO OUTSOURCED SERVICES.....	15
14. RISK EVALUATION AND MEASUREMENT	15

14.1 Framework for risk evaluation.....	16
14.2 Area of risk evaluation	16
15. PERIODIC RISK ASSESSMENT, AUDIT AND REVIEWS	17
15.1 Review of outsourcing arrangements	17
16 OTHER REGULATORY REQUIREMENTS	18
17. REPORTING TO INDIAN BANKS ASSOCIATION.....	18

1. BACKGROUND

Utkarsh Small Finance Bank Limited is a wholly owned subsidiary promoted by Utkarsh Core Invest Limited formerly known as Utkarsh Micro Finance Limited. It aims to provide affordable & accessible banking services which are process centric, technology enabled, and people oriented resulting in reliable, scalable, and sustainable institution facilitating socio-economic changes. The purpose is to provide Banking products to the unserved and underserved sections of the country, which includes small and marginal farmers, micro and small industries, and other organized sector entities, at an affordable cost. The Bank's vision is "To be the most trusted, digitized bank that is financially and socially inclusive, and creates value across social strata through insightful and viable solution".

Bank engages service provider to manage certain activities, on behalf of/ for the Bank, on a continual basis that includes activities like data processing, business correspondents, DSA, etc., these are governed by RBI guidelines viz. DBOD.NO.BP.40/21.04.158/2006-07 "Guidelines on Managing Risk and Code of Conduct in Outsourcing of Financial Services by Bank" dated November 3, 2006, and further instructions issued vide guideline DBR.No.BP.BC.76/21.04.158/2014-15 issued on March 11, 2015.

2. DEFINITION

i) Outsourcing: 'Outsourcing' can be defined as Bank's use of a service provider (either an affiliated entity within group or an entity that is external to the group) to perform activities on a continuous basis that would normally be undertaken by the Bank itself, through a legal agreement.

a) Financial Outsourcing - Typical activities under Financial Outsourcing includes, Application Processing (Loan Origination, Credit Card), Document processing, Marketing and research, Supervision of loans, Data processing and Back office related activities etc."

b) IT Services outsourcing - Common areas under technology operations includes, Technology Infrastructure Management, Maintenance and Support, Application Development, Maintenance and Testing etc. Areas related to Information Security Operations, Support in various IT areas like Services, Applications, Software, Hardware, Network etc. and Database management and various type of support services etc.

c) Non-Financial Outsourcing - Outsourcing arrangements like courier, Security services, Janitorial services would be considered as non-financial outsourcing and would be kept out of the purview of this policy as the Bank would not have undertaken this activity under the normal course.

ii) Sub-Contracting - Subcontracting refers to an arrangement whereby the outsourced agency engaged by the Bank further outsources a part of its activity to another service provider (Sub contractor).

3. APPLICABILITY

This policy would govern the broad principles and process adopted for appointment of service provider for outsourcing of financial activities and technology operations in the Bank. For this policy, service provider would include Group entities of the Bank.

Activities outsourced to a service provider would be governed by this policy and respective guidelines issued by the country related to such activities through its regulators. In cases of difference between this policy and guidelines of the country the more stringent of the two would prevail.

4. ACTIVITIES THAT CANNOT BE OUTSOURCED

Bank shall not outsource any activities which are prohibited under applicable legal, regulatory or statutory requirements. Bank through the Outsourcing committee would ensure that activities like, Core management functions viz., Internal audit and the Compliance function, execution of orders and monitoring of trading activities of clients, decision - making functions like determination of compliance with KYC norms for opening deposit accounts, according sanction for loans (including retail loans) and management of investment portfolios are not outsourced.

Core Business Functions are functions which are vital functions without which an organisation cannot survive and/ or effectively achieve its objectives. These functions are specific to the organisation and help it differentiate from competition and involve decision making at the highest levels. These functions may include functions like Business Strategy, Pricing -Client services, Client Relationship Management, Product Design and Management, Management of Intellectual Property. Board may approve outsourcing of core business activities or functions on the basis the business benefits after Risk Management committee has evaluated associated risks and other factors as laid down in the policy.

Outsourcing arrangements like courier, security services, and janitorial services would be considered as non-financial outsourcing and would be kept out of the purview of this policy, as the Bank would not have undertaken this activity under the normal course.

5. COMMON AREAS OF OUTSOURCING

Financial and Technology Outsourcing - Outsourcing Arrangements, which would ideally have been carried out by Bank in normal course, being entrusted to other agency due to a specific reason. All financial and Technology Services outsourcing would be under the purview of the policy irrespective of its material impact. Typical activities under financial outsourcing and technology operations includes

a) Banking Operations

- i) Sourcing Leads generation.
- ii) Application processing (Loan Origination, Credit Card).
- iii) Supervision of loans.
- iv) Cash management and Collections.
- v) Customer service helpdesk/ call center services.
- vi) Document/ Data/ Transaction Processing including payments, loans, deposits.
- vii) Activities such as Debit card printing and dispatch, verifications.
- viii) Back office related activities etc.

- ix) Marketing and research.
- x) Fiduciary and trading activities.

b) Technology Operations

- i) Technology infrastructure management, maintenance and support.
- ii) Application development, maintenance and testing.

6. FRAMEWORK FOR APPROVAL

Proposals for outsourcing an activity, half year review of the outsourced activity and annual review of the service providers would be carried out by the Committee set up for this purpose.

Bank would constitute a Committee which would assess, quantify, and review the risk mitigations measures being put in place for outsourced financial and technology services irrespective of the materiality. Bank through the relevant department, will have the ultimate responsibility for the outsourced activity. The outsourcing of any activity would not diminish the obligation of the Bank in respect of that activity. The roles and responsibilities and the composition of the Committee are described below:

Members: Roles and Responsibilities

Members	Roles and Responsibilities
Head –Operations (Chairperson)	To examine the aspects relating to operations. The Chairperson to ensure that the management committee functions properly, that all relevant matters are discussed and that effective decisions are made and carried out. He also co-ordinate the committee to ensure that appropriate policies and procedures are in place for effective management of the organisation.
Head – Branch & Assets Operations (Convener)	To coordinate for convening the meeting and functionality maintain record and all documentation related to on boarding and reviews.
Chief Financial Officer (CFO)	Evaluation of financial soundness of the outsourced agency.
Chief Information Officer (CIO) / Suitable nomination from IT	Examine the aspects relating to information technology services and operations.
Chief Compliance Officer (CCO)	Examine the regulatory impact including statutory compliance and

	convey the regulations to be complied with. Provide appropriate clauses in the service level agreement to cover all the necessary regulatory and risk mitigation measures in line with Bank's Outsourcing Policy.
Chief Human Resource Officer (CHRO)	To examine the human aspects relating to Onboarding outsource vendor partners.
Chief Information Security Officer (CISO)	Examine the aspects relating to Information Security services and operations.
Chief Risk Officer (CRO)	To evaluate proposals from a Risk perspective and furnish his inputs wherever the Bank is outsourcing any of its activities

HODs having Outsourced activities (Participate as presentee)	Arrange for Onboarding and managing the service providers including review of outsourcing contracts as per defined frequency (Annually/ Half yearly) and submission to Outsourcing committee.
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7. ROLE AND RESPONSIBILITY OF OUTSOURCING COMMITTEE

7.1 Regulatory and Supervisory requirements

Bank would not engage in outsourcing an activity that may result in compromising or weakening of internal controls, business conduct or reputation. All outsourcing arrangements would adhere to the following broad guidelines that should be monitored by the Outsourcing committee during reviews.

i. Compliance to all relevant laws, regulations, guidelines, and conditions of approval, licensing, or registration etc., are fulfilled.

ii. Outsourcing arrangements would not affect the customer's right against the Bank, including the ability of the customer to obtain, redress as applicable under relevant laws.

iii. Outsourcing arrangement, whether with service provider located in India or abroad will not impede or interfere with the Bank's ability to effectively oversee and manage the service provider's activities nor should it impede the Reserve Bank of India in carrying out its supervisory functions and objectives. Outsourcing agreement should include clause to recognise the right of the Reserve Bank to cause an inspection of a Bank and/or service provider of a bank and its books and account its documents, records of transactions, and other necessary information given to, stored or processed by the service provider within a reasonable time by one or more of its officers or employees or other persons.

iv. The grievance redressal mechanism in the Bank would in no way be compromised on account of outsourcing.

v. Service Provider, if it is not a subsidiary of the Bank would not be owned or controlled by any director or officer/employee of the Bank or their relatives having the same meaning as assigned under the Companies Act 2013.

vi. Outsourcing arrangements should be made in due compliance with the existing statutory and regulatory provisions.

vii. Service Provider employs the same high standard of care in performing the outsourced activity as would have been employed by the Bank.

viii. Outsourcing of services relating to credit cards would be as per the detailed instructions contained in RBI Circular (DBOD. FSD. BC. 49/24.01.011/2005-06 dated 21st November 2005) and RBI guidelines on engagement of recovery agents conveyed vide DBOD.No.Leg.BC.75/09.07.2005/2007-08 dated April 24, 2008. The code of conduct for Direct Sales Agents (DSAs) will be as per "Model code of conduct for DSAs circulated by IBA.

7.2 Due diligence measures to be adopted

Comprehensive due diligence on the nature, scope and complexity of the outsourcing should be performed. Identify the key risk and risk mitigation strategies. e.g. in case of technology outsourcing, the state of security practices and controls environment offered by the service provider is a key factor.

Outsourcing agreement should include, oversight and management of third-party vendor's/ service providers & partners as a due diligence measure the agreement should also have at least following provisions.

i. Nature of legal relationship between the parties – i.e., whether agent, principal or otherwise. The contract should clearly define what activities are going to be outsourced including appropriate service and performance standards.

ii. The Outsourcing and Vendor risk management team must ensure that Bank can access all books, records, and information relevant to the outsourced activities available with the service provider.

iii. The contract should provide for continuous monitoring and assessment by the bank of the service provider so that any necessary corrective measure can be taken immediately.

iv. The outsourcing agreement should provide provision for the preservation of documents and data by the service provider in accordance with the legal/regulatory obligation of the bank in this regard.

7.3 Due diligence of service provider

During the process of negotiating/ renewing an Outsourcing arrangement due diligence should be performed to assess the capability of the service provider to comply with obligations in the outsourcing agreement. Due diligence should involve an evaluation of all information about the service provider including qualitative, quantitative, financial, operational, and reputational factors as follows:

- i. Past experience and competence to implement and support proposed activities over the contractual period.
- ii. Financial soundness and ability to service commitments even under adverse conditions.
- iii. Business reputation and culture, compliance, complaints and outstanding or potential litigations.
- iv. Security and internal control and monitoring environment, business continuity management
- v. External factors like political, economic, social, and legal environment of jurisdiction in which the service provider operates and other events that may impact service Performance.
- vi. Due diligence for sub-service providers.
- vii. Risk management, framework, alignment to applicable international standards on quality/security/environment etc., may be considered.
- viii. Secure infrastructure facilities.
- ix. Employees training and knowledge transfer.
- x. Reliance on and ability to deal with sub-contractors.

Extent of due diligence reviews may vary based on risk inherent in the outsourcing arrangements. Due diligence undertaken during the selection process should be documented and re-performed periodically as part of the monitoring and control processes of outsourcing. Outsourcing and Vendor risk management team should ensure to obtain independent reviews and market feedback to supplement internal findings. Outsourcing and Vendor risk management team should ensure that information used for due diligence is current and not more than 12 months old.

8. OUTSOURCING AGREEMENT

The Outsourcing can be done only after execution of the agreement between the Bank and vendor. Agreement with the service provider would be executed as per standard format and any deviation should require a specific approval by the Outsourcing Committee. Amendments to the agreement should be carried out as a supplementary to the agreement.

The terms and conditions governing the contract between the bank and the service provider should be carefully defined in written agreements and vetted by bank's legal counsel on their legal effect and enforceability.

- i. Outsourcing Committee should ensure that the contract brings out nature of legal and regulatory relationship between the parties (agent, principal or otherwise), and addresses risks and mitigation strategies identified at the risk evaluation and due diligence stages. Contracts should clearly define the roles and responsibilities of the parties to the contract and include suitable indemnification clauses. Any 'limitation of liability' consideration incorporated by the service provider should be assessed in consultation with the legal department.
- ii. Contracts should provide for periodic renewal and re-negotiation to enable the Bank to retain an appropriate level of control over the outsourcing and should include the right to intervene with appropriate measure to meet the Banks' legal and regulatory obligations.
- iii. The contract must enable the Bank with the ability to access all books, records and information relevant to the outsourced activity available with the service provider.
- iv. The contract should provide the bank with the right to conduct audits on the service provider whether by its internal or external auditors, or by agents appointed to act on its behalf and to obtain

copies of any audit or review reports and findings made on the service provider in conjunction with the services performed for the bank.

v. The contract should include clauses to allow the Reserve Bank of India or persons authorized by it to access the Bank's documents, records of transactions, and other necessary information given to, stored or processed by the service provider within a reasonable time.

vi. The contract should also include clause to recognize the right of the Reserve Bank to cause an inspection to be made of a service provider of a bank and its books and account by one or more of its authorized officers or employees or other persons.

8.1 Termination clause

i. Contracts should include a termination clause and minimum periods to execute a termination provision, as deemed necessary.

ii. Agreements should provide for maintaining confidentiality of customer's information even after the contract expires or is terminated by either party.

iii. Contract should include conditions for default termination/ early exit option for contracts. This may include circumstances when the service provider undergoes a change in ownership becomes insolvent or goes under liquidation, received judicial indictment (whether within India or any other location) or when there has been a breach of confidentiality, security, or demonstrable deterioration in quality of services rendered.

iv. In all cases of termination (early or otherwise) an appropriate handover process for data and process needs to be agreed with the service provider.

In the event of termination of the agreement for any reason, it should be adequately publicized to ensure that the customers do not continue to entertain the service provider. List of terminated cases and IBA caution list would be uploaded on the Bank's website and intranet. Business Heads should ensure that service of outsourced agencies which are included in 'Caution List' of Indian Banks Association should not be availed.

8.2 Sub-Contracting

Agreements may include covenants limiting further sub-contracting. Agreements should provide for due prior approval/consent by the bank of the use of subcontractors by the service provider for all or part of an outsourced activity. The bank should retain the ability of similar control and oversight over the sub service provider as the service provider.

8.3 Dispute resolution: Agreements should specify the resolution process, the event of default, indemnities involved and the remedies and recourse of the respective parties to the agreement.

8.4 Applicable laws: Agreements should include choice of law provisions, based on the regulations as applicable to the bank. An agreement should be tailored to provide for specific risks relating to cross border businesses and operations, data privacy and ownership aspects among others.

9 OUTSOURCING OFF-SHORE AND WITHIN A GROUP

9.1 Off-shore Outsourcing of financial services (Outsourcing to Foreign Service providers)

9.1.1 The engagement of service providers across multiple geographies

The engagement of service providers across multiple geographies exposes the Bank to country risk – economic, social and political reasons in the country that may adversely affect the Bank business and operations such conditions and events could prevent the service provider from carrying out the terms of its agreement with the bank. To manage the country risk involved in such outsourcing activities, Outsourcing and Vendor risk management team should take into account and closely monitor government policies and political, social, economic and legal conditions in countries where the service provider is based, during the risk assessment process and on a continuous basis and establish sound procedures for dealing with country risk problems. This includes having appropriate contingency and exit strategies.

Outsourcing Committee should ensure the following:

- i. Bank should principally enter arrangements with parties operating in jurisdictions that generally uphold confidentiality clauses and agreements. The governing law of the arrangement should also be clearly specified.
- ii. Bank should not outsource within jurisdictions where access to books, records and any other information required for audit and review purposes may be impeded due to regulatory or administrative constraints.
- iii. It should notify the Regulator where the rights of access for the Bank and/ or the Regulator are likely to be impeded.
- iv. Emerging technologies such as data centre hosting, applications as a service, cloud computing have given rise to unique legal jurisdictions for data and cross border regulations. Banks should clarify the jurisdiction for their data and applicable regulations at the outset of an outsourcing arrangement. This information should be reviewed periodically and in case of any significant changes performed by the service provider.

9.1.2 The activities outsourced outside India

The activities outsourced outside India should be conducted in a manner so as not to hinder efforts to supervise or reconstruct the Indian activities of the bank in a timely manner.

9.1.3 The outsourcing related to overseas operations of Bank

The outsourcing related to overseas operations of bank would be governed by both these guidelines and the host country guidelines. Where there are differences, the more stringent of the two would prevail. However, where there is any conflict, the host country guidelines would prevail.

9.2 Outsourcing within a group

These guidelines are generally applicable to outsourcing within a group conglomerate, including Head Office, Zonal Office/Regional office, Administrative offices or Branch office of the company whether located within or outside India. These requirements may be addressed as part of group wide risk assessment and management procedures.

Due diligence on an intra-group service provider may take the form of evaluating qualitative aspects on the ability of the service provider to address risks specific to the Bank.

10 CONTROL ENVIRONMENTS OFFERED BY THE SERVICE PROVIDER

Outsourcing and Vendor risk management team should ensure to evaluate the adequacy of internal controls environment offered by the service provider. Due consideration should be given to the implementation of following by the service provider:

- i. Information security policies and employee awareness of the same.
- ii. Controls implemented for logical access to customer information by service provider staff, so that information may be accessed on a need-to-know basis only.
- iii. Physical and environmental security and controls.
- iv. Network security and controls.
- v. Formal process for tracking and monitoring program changes and projects.
- vi. Process for incident reporting and problem management.
- vii. Special control considerations for service providers using cloud computing as part of service.
- viii. Control considerations for handling of customer information and personally identifiable Information.
- ix. Data classification and controls for handling data.

10.1 Confidentiality and security:

- i. Outsourcing agreement should mandate controls to ensure customer data confidentiality and service provider's liability in case of breach of security and leakage of confidential customer related information. e.g., use of transaction-enabled mobile banking channels necessitates encryption controls to ensure security of data in transmission.
- ii. Outsourcing agreement should mandate controls to provide for the preservation of documents and data by the service provider in accordance with the legal/regulatory obligation of the bank in this regard.

10.2 Responsibilities of DSA/DMA/ recovery agents

Relevant department hiring DSA/ DMA/ Recovery agents would ensure the following:

- i. Direct Sales Agents (DSA)/ Direct Marketing Agents (DMA)/ Recovery Agents are trained to handle customers with care and sensitivity, particularly while soliciting customers by adhering to hours of calling, maintain privacy of customer information and convey the terms and conditions of the products.
- ii. Recovery Agents adheres to instructions on Fair Practices Code for lending (Circular DBOD. Leg. No. BC.104/09.07.007/2002-03 dated 5th May 2003) as also their own code for collection of dues.
- iii. Recovery agents should refrain from action that could damage the integrity and reputation of the Bank and would observe strict customer confidentiality.
- iv. Recovery Agents do not resort to intimidation or harassment of any kind either verbal or physical against any person in their debt collection efforts

Department outsourcing the activity, should ensure that any deviations from the above-mentioned terms are updated to Outsourcing Committee within 7 days along with the details of the incident and action taken against the service providers.

11. MONITORING AND CONTROL OF OUTSOURCED ACTIVITIES

11.1 Structure for management and control of Outsourcing

Outsourcing Committee should ensure to establish a structure for management and control of outsourcing, based on the nature, scope, complexity and inherent risk of the outsourced activity. A structure for monitoring and control outsourced activities should comprise of the following:

- i. A centralized record of all material outsourcing, including technology outsourcing and sub service provider relationships, that is readily accessible for review by the Board and Senior Management of the bank should be maintained. The records should be updated promptly, and half yearly reviews should be placed before the Board.
- ii. Outsourcing Committee should review and monitor the security practices and control processes of the service provider on a regular basis and require the service provider to disclose security breaches.
- iii. Outsourcing Committee should ensure to pro-actively intimate RBI of any adverse developments or non-compliance with legal and regulatory requirements in an outsourcing arrangement.

11.2 Service level agreements and performance metrics

Outsourcing Committee should ensure to include SLAs in the outsourcing contracts to agree and establish accountability for performance expectations. SLAs must clearly formalize the performance

criteria to measure the quality and quantity of service levels. Outsourcing Committee should arrange to develop the following towards establishing an effective oversight program:

- i Formal policy that defines the SLA program.
- ii SLA monitoring process.
- iii Recourse in case of non-performance.
- iv Escalation process.
- v Dispute resolution process.
- vi Conditions in which the contract may be terminated by either party.

11.3 Measuring by key performance indicators (KPIs)

Bank should develop certain performance indicators under both normal and contingency circumstances for the services provided by the Service Provider and would assess the performance based on those indicators. Frequency of the assessment would also be allocated to each of the indicators for better management. Provisions need to be in place for timely and orderly intervention and rectification in the event of substandard performance by the service provider. The KPIs would mainly cover the service quality aspects, timely report submission by the service provider etc. The results of the KPIs would be shared with the Outsourcing Committee on an Annual basis for perusal and action required, if any.

Operations department would maintain record of all financial and technology outsourcing that is readily accessible for review by the Board and Senior Management of the Bank.

12. BUSINESS CONTINUITY AND MANAGEMENT OF DISASTER RECOVERY PLAN

Outsourcing Committee should ensure that Bank's business continuity preparedness is not adversely compromised on account of outsourcing. Outsourcing Committee should adopt sound business continuity management practices as issued by RBI and seek proactive assurance that the outsourced service provider maintains readiness and preparedness for business continuity on an ongoing basis.

a) Department outsourcing critical activities should ensure that the activity happen in an uninterrupted way without causing any disruption to the Bank or its customers. Towards this end, concerned department should ensure the following before outsourcing:

- i. Service providers have a good framework for documenting, maintaining, and testing business continuity and recovery procedures. Relevant department may also conduct occasional joint testing and review the activities of service provider.
- ii. Relevant department should retain an appropriate level of control over their outsourcing and the right to intervene.
- iii. With appropriate measures to continue operations in unexpected scenarios, without incurring prohibitive expenses and without any break in the operations of the Bank and its services to the customers.

iv. The Outsourcing agreement should contain clauses for contingency plans and testing thereof, to maintain business continuity.

v. Outsourcing often leads to the sharing of facilities operated by the service provider. The Outsourcing Committee should ensure that service providers are able to isolate the bank's information, documents, and records and other assets. This is to ensure that in adverse conditions, all documents, records of transactions and information given to the service provider and assets of the bank can be removed from the possession of the service provider to continue its business operations, or deleted, destroyed, or rendered unusable.

vi. Outsourcing Committee should ensure while framing the viable contingency plan, To consider the availability of alternative service providers or the possibility of bringing the outsourced activity back-in house in an emergency (for example, where number of vendors for a particular service is extremely limited) and the costs, time and resources that would be involved and take suitable preparatory action.

13 GRIEVANCES RELATING TO OUTSOURCED SERVICES

Outsourcing Committee should ensure to constitute a Grievance redressal machinery within the bank and give wide publicity about it through electronic and print media.

Customers of the Bank can lodge a complaint against the service provider/ employee of the service provider through the customer grievance channel. Relevant department should maintain data of all such complaints and submit the same to the Outsourcing committee. The Outsourcing committee should factor in these complaints during their review.

Below are few points that must be included in Grievance redressal machinery

i. The name and contact number of designated grievance redressal officer of the Bank should be made known and widely publicized. The designated officer should ensure that genuine grievances of customers are redressed promptly without involving delay. It should be clearly indicated that Bank's grievance redressal machinery will also deal with the issue relating to services provided by the outsourced agency.

ii. A time limit of 30 days may be given to the customers for preferring their complaints/ grievances. The grievance redressal procedure of the Bank and the time frame fixed for responding to the complaints should be displayed on the Bank's website.

iii. If a complainant does not get satisfactory response from the Bank within one month from the date of his/her lodging the complaint with the Bank, he/she will have the option to approach the Office of the concerned Banking Ombudsman for redressal of his/her grievance/s.

14. RISK EVALUATION AND MEASUREMENT

Risk evaluation should be performed prior to entering into an outsourcing agreement and reviewed periodically in the light of known and expected changes as part of the strategic planning or review processes.

14.1 Framework for risk evaluation

Risk evaluation framework should include the following steps:

- i. Identification of role of outsourcing in the overall business strategy and objectives and inter-linkages with corporate strategic goals.
- ii. Analysis of impact of such arrangement on the overall risk profile of the bank and whether adequate internal expertise and resources exist to mitigate the risks identified.
- iii. Analysis of risk-return on the potential benefits of outsourcing vis-à-vis the vulnerabilities that may arise. Banks should evaluate vendor managed processes or specific vendor relationships as they relate to information systems and technology. All outsourced information systems and operations may be subject to risk management and security and privacy policies that meet the Bank's own standards.

14.2 Area of risk evaluation

Before deciding on outsourcing any service, CISO and the respective function heads shall evaluate the risks associated with the activities to be outsourced and consider the same for outsourcing only if the risks are acceptable. The respective function heads along with CISO shall identify and implement mitigation plan for all the high & medium risks being accepted and suggest suitable mitigates:

- i. **Strategic Risk** - Service provider may conduct the business on its own behalf, which may be inconsistent with the overall
- ii. I strategic goals of the Bank.
- iii. **Reputation Risk** - Poor quality of service and customer interaction by service provider may not be as per the standards of the Bank.
- iv. **Compliance Risk** - Privacy, Consumer and Prudential laws may not be adequately complied by the service provider.
- iv. **Operational Risk** - Technical failures, fraud, errors, inadequate financial capability of service provider to meet obligations/provide remedies may cause such risks.
- v. **Legal Risk**- Exposure to fines, Penalties, or Punitive damages resulting from supervisory actions as well as private settlements due to omissions and commissions of the service provider etc.
- vi. **Exit Strategy Risk** - This may arise from over-reliance on one firm, loss of relevant skills in the Bank itself might prevent it from bringing the activity back in-house.
- vii. **Counter party Risk** - Due to inappropriate underwriting or credit assessments.

viii. Country Risk - Due to political, social or legal climate creating added risk.

ix. Contractual Risk - It may arise due to circumstantial difficulty in enforcing a contract.

x. Concentration and Systemic Risk - It may arise when a number of Banks have considerable exposure to one service provider.

15. PERIODIC RISK ASSESSMENT, AUDIT AND REVIEWS

Outsourcing Committee should ensure to conduct pre and post outsourcing implementation reviews and also review its outsourcing arrangements periodically to ensure that its outsourcing risk management policies, procedures and guidelines are effectively complied with.

Outsourcing Committee should also ensure to periodically commission independent audit and expert assessments on the security and control environment of the service provider, such assessments and reports on the service provider may be performed and prepared by the Bank's internal or external auditors or by agents appointed by the Bank.

Such reviews should take adequate cognizance of historical violations or issue remediation during previous audits and assessments. Copies of previous audits and assessments should be shared during RBI inspections.

15.1 Review of outsourcing arrangements

Outsourcing Committee should review the financial and operational condition of the service provider to assess its ability to continue to meet outsourcing obligations. Such due diligence reviews, which can be based on all available information about the service provider including reports by the service provider's external auditors. Any deterioration or breach in performance standards, confidentiality and security and its business continuity preparedness should be highlighted in the review.

Outsourcing Committee should carry out half yearly review of all outsourcing arrangements as on 30th June of every year and, an annual review of all service providers along with the activity review as on 31st December of every year.

Review would be conducted within time frame of 3 months. The review report along with the observations & action taken should be submitted to the subsequent Risk Management Committee of the Board.

Half Yearly Review (Off-site) - A half yearly review of the operational risk associated with the services provided by the Service Provider should be undertaken to assess its ability to continue to meet its outsourcing obligation by the competent team of the Bank. This review would be based on checklist and self-certification by the Service Provider. A consolidated report on the findings of the review undertaken by the concerned department of the Bank will be put up to Outsourcing Committee of the Bank and to the respective departments to whom the function is outsourced for perusal and action required, if any.

Annual Review (On-site) – The department responsible for Outsourcing the activity of the Bank should conduct the on-site review of the activities provided by the Service Provider. The review would be based on sample testing at the site of the Service provider. Report on the findings of the review undertaken by the officer of the Bank should be put up to the Outsourcing Committee of the Bank and to the respective departments to whom the function is outsourced for perusal and action required, if any

16. OTHER REGULATORY REQUIREMENTS

Following regulatory requirements are to be fulfilled by the relevant departments before outsourcing an activity to the service provider.

i. Service Provider should seek prior approval of the Bank (relevant department, outsourcing the activity) for use of sub-contractors for all or any part of the outsourced activity. Relevant department should ensure that the sub-contracting arrangements are compliant with the extant regulatory guidelines on outsourcing.

ii. In cases like outsourcing of cash management services, involving reconciliation of transactions, service provider/sub-contractor should ensure that reconciliation of transactions between the Bank and service provider (and/ or its subcontractor) are carried out in a timely manner.

iii. An ageing analysis of such entries pending reconciliation with outsourced service providers should be placed before the Audit Committee of the Board (ACB).

iv. Internal audit department should conduct an audit of outsourced activities and submit the report to ACB.

v. Internal audit department would submit an 'Annual Compliance Certificate' giving particulars of outsourcing contracts, periodicity of audit by internal/ external auditor, major findings of the audit and action taken through Board, to the Chief General Manager in-Charge, Department of Banking Supervision, Central Office, Reserve Bank of India, Mumbai.

All products literature/ brochures etc. should have a clause stating that Bank may use the services of agents in sales/ marketing etc., of the products. The role of agents, if any should also be indicated in broad terms.

17. REPORTING TO INDIAN BANKS ASSOCIATION

Outsourcing Committee should ensure reporting of required information to below authority:

i. Indian Banks Association (IBA) – All cases for 'termination for cause' have to be reported by concerned departments to Outsourcing committee and Outsourcing committee shall intimate to Compliance department for inclusion in IBA caution list.
