

**FEDERAL RESERVE BANK
OF NEW YORK**

AT-10775(c)
March 29, 1995

OUTSOURCED SERVICE ARRANGEMENTS

*To the Chief Executive Officers of all State Member Banks,
Branches and Agencies of Foreign Banks, and Edge Corporations
in the Second Federal Reserve District:*

Banking institutions are increasingly turning to affiliated and non-affiliated institutions to provide services to them. Such "outsourced" services include computer processing and accounting services provided under service contracts, but also include other banking services as described more fully below.

Regulatory Update

When a banking institution contracts for outside services, Section 7 (c) (2) of the Bank Service Corporation Act requires the contracting institution to notify the appropriate Federal banking agency. During recent examinations by the Federal Reserve Bank of New York, we have encountered a number of instances where outsourcing arrangements had not been reported to us.

This notice is intended to remind institutions of the reporting requirements of the Bank Service Corporation Act, and also to update our files as to existing outsourcing arrangements covered by the Act. In order to accomplish the latter, this Bank is requesting that all institutions for which it is the primary supervisor provide a listing of all current arrangements in place for outsourced bank services. The information reported will assist us in planning our future examinations. It should also help expedite the examination process when we are on site.

During an examination, an examiner will be looking for a clearly written contract and an evaluation of the perceived risks for each outsourced service. For material outsourced services, the basis for the selection of the servicer should also be included along with periodic updates indicating the viability of the servicer. When the service is critical to the institution, or has significant operational or other risks, files should also support insurance considerations, audit coverage, contingency operating plans, and any other steps taken to address the unique characteristics of the service.

Guidelines for Providing Information

For all existing service arrangements, please provide:

- the name and address of each service provider;
- the nature of each service;
- the contractual and financial arrangements under which the service was established; and
- the date the arrangement began.

The nature of each service should be described as specifically as possible. For example, computer services may include more than one application (e.g., deposits, loans, payroll, investments, and trading). Also, a single organization, such as a loan company, may provide more than one type of service (e.g., bookkeeping, computer processing, custody, and payment collection). Where an organization provides more than one service, they should all be listed.

In responding to this request, we ask that you include all bank services performed for your institution by any other entity except for services provided under loan participations or similar agreements with banks. Services provided by an affiliate should be listed separately from those provided by third parties. While the term "bank services" is somewhat broad, the following list offers some guidance for the type of services that should be reported:

- Accounting (taxes, payment/interest calculation)
- Asset appraisal
- Auditing (excluding statutory audits such as 10K preparation and directors examinations)
- Bookkeeping ("back office" operations including transaction and account recordkeeping)
- Computer processing
- Custody (investments, cash, documents)
- Disaster recovery facilities
- Document collection/custody (legal, insurance)
- Electronic banking (ATMs, point-of-sale)
- Investment powers (discretionary)
- Market valuation (pricing)
- Payment collection (regular, delinquent)
- Payments processing (funds transfer, securities settlement, ACH)
- Record storage

Responses are requested by June 1, 1995. If your institution has no outsourcing arrangements, please respond by indicating that you have none.

Questions, as well as your response, should be directed to:

Joseph L. Galati II, Manager (Tel. No. 212-720-7946)
Advisory and Technical Services Function
Bank Supervision Group
Federal Reserve Bank of New York
33 Liberty Street
New York, NY 10045

Future Reporting

If your institution enters into or terminates any bank service arrangement in the future, please notify this Bank within 30 days, as required by Section 7 (c) (2) of the Bank Service Corporation Act.

CHESTER B. FELDBERG,
Executive Vice President.