Outsourcing Policy

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OUTSOURCED SERVICES

EXECUTIVE SUMMARY

Aim & Introduction

This policy applies to MyState Limited and all Group subsidiaries.

MYS for the purpose of this policy equally means MyState Limited and all Group subsidiariesin so far as these companies are required to comply with the APRA CPS 231 requirements and as Australian Financial Services (AFSL) and Australian Credit (ACL) licensees.

The aim of this Policy is to outline prudent practices in relation to the management of the Group's outsourcing arrangements consistent with the requirements of APRA Prudential Standard – CPS 231 Outsourcing. This policy also draws on the requirements of CPS 510– Governance and PPG 511 – Remuneration.

Adherence to this policy will ensure that the operational and financial risks associated with outsourcing arrangements are properly managed. The policy also ensures that outsourcing arrangements are subject to appropriate due diligence, approval and on-going monitoring.

While responsibility for the day-to-day management of outsourced activities may reside with the company to whom the activity is outsourced, MYS remains accountable for the activity and must therefore assess and manage the risks associated with outsourcing appropriately.

POLICY PARAMETERS

Key Terms

MYS policy adopts key terms as defined in *Prudential Standard APS 001 Definitions*, and *Prudential Standard CPS 231 Outsourcing.*

Material means a 'material business activity' that has the potential, if disrupted to have a significant impact on MYS's business operations or its ability to manage risks effectively, having regard to such factors as:

(a) The financial and operational impact and impact on reputation of a failure of the service provider to perform over a given period of time;

(b) The cost of the outsourcing arrangement as a share of total costs;

(c) The degree of difficulty, including the time take, in finding an alternative service provider or bringing the business activity in house;

(d) The ability of MYS to meet regulatory requirements if there are problems with the service provider;

(e) Potential losses to the regulated institutions' customers and other affected parties in the event of a service provider failure; and

(f) Affiliation or other relationship between the MYS and the service provider.

For the purposes of this Policy, the internal audit function is a material business activity.

Where there is doubt as to whether a business activity that is to be outsourced would be regarded as material, managers must consult with their Executive or Senior Manager for guidance and advice.

Offshoring means the outsourcing by MYS of a material business activity associated with its Australian business to a service provider (including a related body corporate) where the outsourced activity is to be conducted outside Australia. Offshoring includes arrangements where the service provider is incorporated in Australia, but the physical location of the outsourced activity is outside Australia. Offshoring does not include arrangements where the physical location of an outsourced activity is within Australia but the service provider is not incorporated in Australia.

Outsourcing involves MYS entering into an arrangement with another party (including a related body corporate) to perform, on a continuing basis, a business activity that currently is or could be undertaken by MYS itself.

Outsourcing Agreement Requirements

All outsourcing arrangements must be undertaken using a written, legally binding agreement. This agreement must be signed by all parties to it before the outsourcing arrangement commences.

At a minimum, the agreement must cover the following areas, details of which are noted in CPS 231. Managers must refer to this Prudential Standard when assessing any outsourcing contract (material or otherwise). A copy of the Prudential Standard can be obtained from the Chief Risk Officer or from the APRA website, www.apra.gov.au .

1. the scope of the arrangement and services to be supplied
2. commencement and end dates
3. review provisions
4. pricing and fee structure
5. service levels and performance requirement
6. audit and monitoring procedures
7. business continuity management
8. confidentiality, privacy and security of information
9. default arrangements and termination provisions
10. dispute resolution arrangements
11. liability and indemnity
12. subcontracting

13. insurance

14. to the extent applicable, offshoring arrangements (including through subcontracting)

15. an indemnity clause to the effect that any sub-contracting by a third-party service provider of the outsourced function will be the responsibility of the third-party service provider, including liability for any failure on the part of the sub-contractor.

16. if MYS enters into an outsourcing arrangement with a related body corporate, a clause to the effect that the Board of MYS must ensure that access to the related body corporate is not impeded.

17. for material outsourcing agreements:

    a. a clause that allows APRA access to documentation and information related to the outsourcing arrangement. In the normal course, APRA will seek to obtain whatever information it requires from MYS, however, the outsourcing agreement must include the right for APRA to conduct on-site-visits to the service provider if APRA considers this necessary in its role as prudential supervisor. APRA expects service providers to cooperate with APRA's requests for information and assistance. If APRA intends to undertake an on-site-visit to a service provider, it will normally inform MYS of its intention to do so.

    b. a confidentiality clause that the service provider will not disclose or advertise that APRA has conducted an on-site visit.

MATERIAL OUTSOURCING AGREEMENTS

Board Approval

All material outsourcing agreements require Board Approval (or ratification in urgent circumstances – see ‘Urgent Action Provisions’ herein). In most cases, Board Approval of material outsourcing agreements will require a two-step process:

Step 1 – In Principle Approval

The appropriate Executive will submit a paper seeking Board Approval in principle to proceed with a detailed tender, due diligence and agreement negotiation process. The required content for this is outlined in "Board Paper Requirements" below.

Step 2 – Execution of Agreement

Present the agreement and findings of the tender and due diligence process (see below for requirement details) to the Board and make a recommendation for the agreement to be executed.

Board Paper Requirements

In addition to the requirements detailed in the Directors policy for Board papers generally, papers submitted for 'In Principle Board Approval' to proceed with an outsourced services tender, due diligence and agreement negotiation process, must also include a risk analysis defined as:

> *A detailed discussion of the risks associated with outsourcing the activity and how these will be mitigated. This will include MYS's contingency plans for Business Continuity in the event the service provider does not or cannot perform.*

In performing a risk analysis, managers may seek assistance from the Chief Risk Officer and/or input from persons with appropriate knowledge and skills including the use of external experts where necessary. The completed risk analysis will be submitted to the Chief Risk Officer for review from the Group perspective prior to submission to the Executive to approve for submission to the Board.

Whilst agreements with outsourced service suppliers may not have a material effect on MYS's financial soundness, those agreement could when considered collectively. As such, the collective risks associated with such arrangements must also be considered as part of the risk analysis, in accordance with PPG 511 – Remuneration.

Selection of Service Providers

If the Board approves, Senior Managers may be granted permission to select a material service provider. Where appropriate, the selection of material service providers will be conducted by a tender process to ensure competitive pricing and suitable candidates.

MYS will specify that a provider will be required to demonstrate capacity in the areas listed in 'Due Diligence'.

DUE DILIGENCE

Once a material service provider has been selected in principle, a comprehensive due diligence process must be undertaken prior to the execution of any contract (except as allowed for in the 'Urgent Action Provisions' herein). The process will draw on the expertise of those with the necessary skills to properly assess the information gathered.

In addition to the items covered in the selection process, the due diligence process will seek to assess the provider's strengths or weaknesses in the following areas with a view to ensuring the long term ability of the provider to continue performing the outsourced activity. The results of the due diligence will be submitted to the Board with the contract proposed for execution. If the Urgent Action Provisions have been invoked, the due diligence results will be submitted to the Board when ratification is sought.

In seeking Board Approval to engage a service provider for the purpose of outsourcing, Management will determine that the provider and any sub-contractors it uses have the qualities listed below. Where the provider or its sub-contractors do not have capacity in the following areas, Management will highlight the fact and provide an explanation as to why the provider is still considered appropriate.

Capacity

MYS will ensure that a potential service provider has the capacity to meet not only MYS's immediate requirements but will cope with growth in operations over the period appropriate to the service.

Record Keeping

Records held by service providers must be adequate for audit trail purposes and must be made readily available to MYS or MYS's auditors and APRA so as to enable effective monitoring of the arrangement.

Confidentiality

Potential service providers must be able to assure MYS of full confidentiality. This also applies to any sub-contractors the service provider may use.

Business Continuity & Disaster Recovery Plans

Any potential service provider of material activities must be able to demonstrate that it has adequate Business Continuity and Disaster Recovery plans. It is preferable that these plans have been either tested or audited by an expert in the field.

Financial Capacity

The service provider must be able to demonstrate a history of stable financial performance and the ability to withstand hardship if necessary.

Technical Ability

This area will cover not only the technical systems and processes of the provider but also the capacity of human knowledge in key areas. If the service provider is reliant on a small number of key people to carry out its operations and those skills are not readily available in the market place, there must be a clear contingency plan in the event those people become unavailable for whatever reason.

Risk Management and Control Framework

MYS will ensure that the service provider has appropriate controls in place to ensure stable performance and compliance with regulatory or legislative requirements. These will include policies and procedures, monitoring and reporting processes, performance standards and internal audits (conducted either internally or by an external firm of auditors).

Insurance

The insurance requirements of individual firms will depend on the type of operations it conducts. However, all providers of material outsourced activities must be adequately insured against the risks they are exposed to. MYS will determine what coverage the firm is likely to require and obtain and hold a copy of the relevant certificate of currency on file. A renewal Certificate of Currency must be obtained annually and held on file.

Offshoring

Where the contractual arrangements involve Offshoring, "MYS must consult with APRA prior to entering into any offshoring agreement involving a material business activity so that APRA may satisfy itself that the impact of the offshoring arrangement has been adequately addressed as part of the MYS's risk management framework".

CONTRACTS

All outsourcing agreements:

1. Must be submitted to Legal & Compliance for internal legal review.

2. Unless executed under the 'Urgent Action Provisions' herein are to be signed in accordance with the MYS Financial Delegations of Authority Policy (Board & Executive) .

3. For material outsourcing agreements, this may only be sought after the appropriate submission for Board Approval has been made.

4. All material outsourcing agreements must be notified to APRA no later than 20 days after execution and will include the notification requirements set out in CPS 231, being a summary of the key risks involved in the outsourcing agreement and risk mitigation strategies put in place to address these risks.

5. Once executed, the arranging Executive, or authorised delegate, will coordinate the notification to APRA through Legal and Compliance and provide original signed contacts and the supporting due diligence material to Compliance for Agreement filing in the register and recording in the Critical Suppliers Register.

Payments to non-employees

In accordance with CPS 510 – Governance and PPG 511 - Remuneration, the following provisions apply to any persons who are not directly employed by MYS but provide outsourced services to the Group and who may, individually or collectively, be able to affect the financial soundness of the institution. Such persons may include but are not limited to, contractors or persons employed by a related service company/provider within a Group or a third-party body corporate.

Where relevant, outsourcing contracts between MYS and a third party must comply with APRA's remuneration requirements. As such, the following provisions must be considered and if relevant, addressed in any outsourcing contract or agreement.

1. Where MYS contracts with third party individuals, the payments to these individuals must conform to the MYS Remuneration Policy.

2. Where MYS contracts with a related body corporate, persons employed by the body corporate who provide services to MYS are to be treated as employees of MYS. As such, payments to these individuals must conform to the MYS Remuneration Policy.

3. Where MYS contracts with an un-related body corporate, it is the contractual terms with the body corporate that are relevant, rather than the remuneration of individuals employed or engaged by the body corporate. In any event, the requirements of the MYS Remuneration Policy must be considered and applied if relevant.

URGENT ACTION PROVISIONS

In order to ensure appropriate management and control of the risks of outsourcing, the process for implementing an outsourcing arrangement is by necessity comprehensive and detailed. Sufficient time must be allowed for the preparation requirements contained herein. However, in case of urgency the following may be applied:

Delegated Authority

In a case of urgency, the Managing Director has the authority to proceed with a material outsourcing contract prior to the requirements for Board Approval being met. However, the following must occur:

1. The Managing Director must receive from the requesting Executive a 'Request to Proceed Urgently' in writing according to the directives outlined in "Urgent Action Requirements" herein.

2. The contract must then be subject to the outcome of a formal Due Diligence process to be undertaken within 60 days of the execution date (unless this has already been undertaken).

3. A full submission containing all of the requirements herein must be made to the Board at the earliest opportunity, for Board ratification of the Managing Director's actions.

4. As far as is possible, the Managing Director will ensure the contract contains an exit clause in the event the Board does not provide ratification.

Urgent Action Requirements

Should urgent action be required, permission may be sought from the Managing Director to proceed without initial compliance with the required detail contained herein for Board submissions. Any such permission sought will be in writing and will include:

1. details of why it is not possible to follow the directives herein.

2. an analysis of the possible consequences of not complying with some or all of the Board submission requirements. This must be prepared by the appropriate Senior Manager in consultation with the Chief Risk Officer and Principal Legal Officer and and must follow the same process as that for policy reviews.

3. details of the consequences of delaying the outsourcing agreement to meet Board submission requirements.

A full submission for Board Approval according to the directives below must be prepared at the earliest opportunity and presented to the Board for ratification of the actions taken under these provisions.

REPORTING & CONTROLS

Management of the outsourcing arrangement

The Manager of the area to which the outsourcing arrangement relates is responsible for monitoring and managing the arrangement.

Once a service provider of a material outsourced activity has been contracted, the responsible Manager will document procedures for the ongoing monitoring of the provider and outsourced arrangement. These procedures will be kept on MYS's Lotus Notes Compliance System.

The responsible Manager will also provide to the Chief Risk Officer a copy of the material outsourced service provider's business continuity plan as well as a copy of MYS's contingency plan for business continuity in the event the service provider cannot perform, originally submitted to the Board. The Chief Risk Officer or their delegate will keep the copies on file in the 'Critical Suppliers Register'. The 'Critical Suppliers Register' will also contain a summary of all the Groups outsourced services.

On a monthly basis (at a minimum or more often if necessary) the responsible Manager will advise the appropriate Executive of the status of the outsourcing arrangements for which they are responsible and will highlight any difficulties, poor performance or material issues.

The Executive Manager will advise the Executive Committee at the earliest opportunity of any significant problem with a material outsourced activity.

Board Reporting

The Board will be kept informed of any significant issues with a material outsourced activity.

Audit

MYS's internal auditors will monitor compliance with the Outsourcing policy on an annual basis.

APRA Reporting

MYS will advise APRA of any significant problems that have the potential to materially affect the outsourcing arrangement, and as a consequence, materially affect the business operations, profitability or reputation of MYS.

When MYS terminates an outsourcing agreement it will notify APRA as soon as practical and provide a statement as to the transition arrangements and future strategies for carrying out the outsourced material business activity.

The Chief Risk Officer will have responsibility for advising APRA of any problems or changes in material outsourcing arrangements.

Contractual Agreement Renewal

Outsourced agreement details will be registered in the Lotus Notes Compliance System, along with agreement expiry or renewal periods.

Prior to agreement expiry, the responsible manager will liaise with the outsourced service supplier to arrange a continuation letter or new contractual agreement. If a new contractual agreement requires execution, the responsible manager will undertake a comparison with the expiring agreement. If there are contractual differences, the new agreement will be subjected to the internal risk review and approval process.