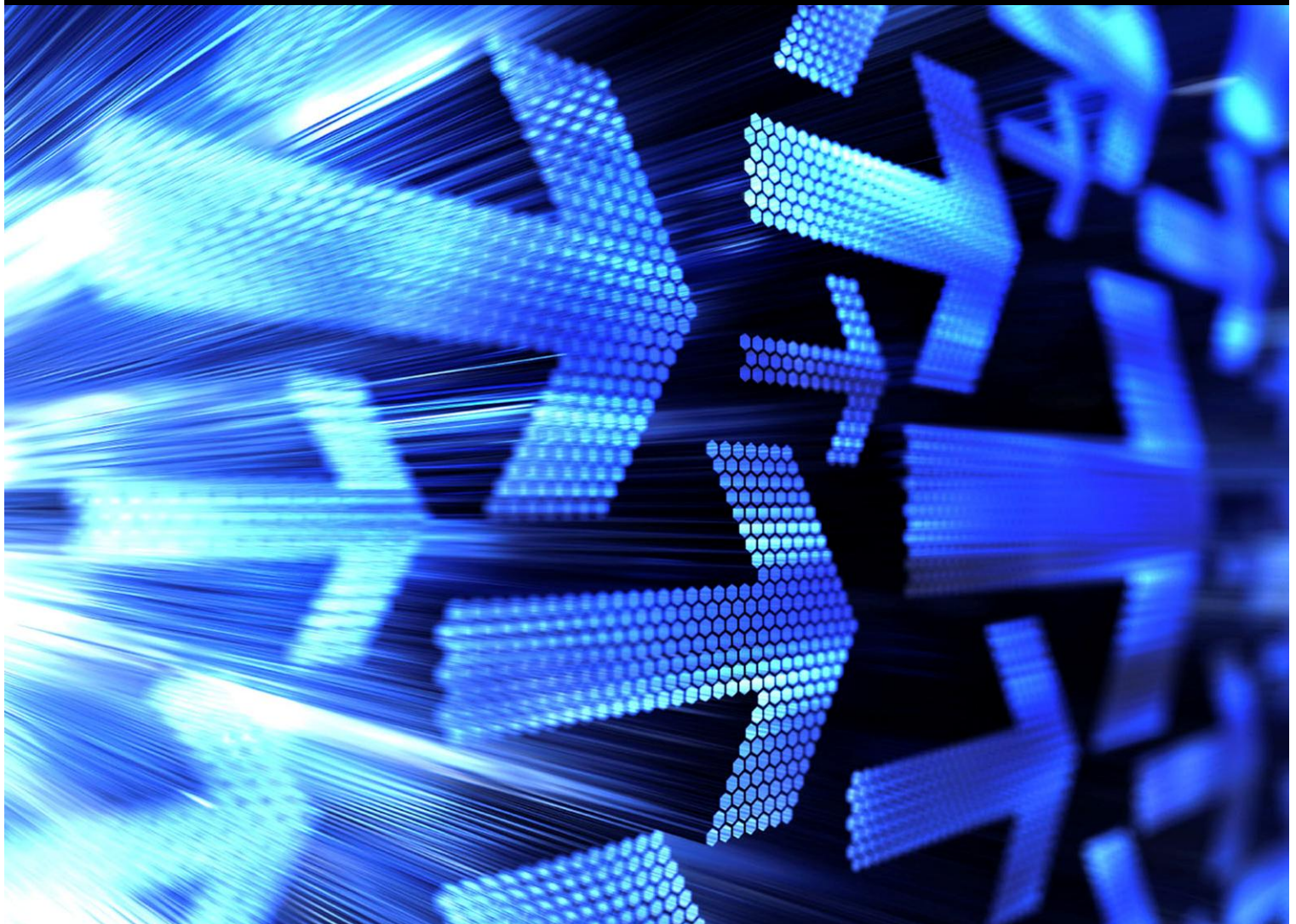


Outsourcing and Financial Institutions Seminar
Three Hats: Customer, Provider, Funder
7 July 2009

OLSWANG



Seminar Summary Notes

Nigel Swycher, Olswang LLP: Chairman's Introduction

Nigel's introduction asked the question: why are we holding an outsourcing seminar in this sector? Outsourcing itself had not in fact significantly altered. However, in the current climate there is a heightened risk that if an outsourcing in this sector goes wrong, the consequences can be very serious. The seminar is therefore an attempt to bring all the current knowledge about outsourcing together in order to ensure that the right considerations are made before outsourcing is undertaken, the best possible outsourcing contract is made and a strong relationship between the provider and the financial institution is developed and maintained.

Phil Brooke, EquaTerra: Outsourcing – where next for financial institutions?

Phil set the scene that there has been a massive change in the Financial Institutions sector; never has there been such turmoil and upheaval. The knee jerk reaction to such trends is the stopping of discretionary spends and, consequently, the main incentive for outsourcing currently is increasingly cost savings. Phil quotes a company director's response to outsourcing, "we are now starting to think the unthinkable": re-assessments of what is a Financial Institution's core business and what is non-core are necessary in this economic climate in order to survive. When approaching the question of whether outsourcing should be part of the strategy to reduce discretionary spend the correct question is not "what shall I outsource?", but "what can I do to capitalise on my organisation's competitive advantages?" and "is outsourcing a part of that?". Outsourcing should not be viewed as a necessary means to cut costs, but an option. If outsourcing contracts already exist there should be continual examination of whether they are "fit for purpose".

However, the economic downturn has also stressed the importance of flexibility and risk/security management. There is a need for greater control over outsourced functions. An outsourcing contract of around five years will tend to provide the requisite balance between flexibility and incentive for vendor investment. Focus on risk will mean that, in the current climate, before an outsourcing contract is made increased due diligence is required not only of the deal, but of the supplier itself more generally, and data security will be emphasised. Thus, cost savings, flexibility and risk and security will shape outsourcing post-credit crunch.

Nigel Swycher, Olswang LLP: Managing the outsourcing lifecycle – not the contract

Nigel stressed that outsourcing required a holistic approach: an outsourcing model requires consideration of "before", "during" and "after" as the needs of an outsourcing relationship are constantly changing.

He asserted that 50% of outsourcing relationships end short of full term. When that statistic is contextualised some outsourcing relationships are ended due to external factors, e.g. M&A consolidation. However, enough of the statistic refers to relationships which have just broken down due to poor management, but this need not be the case. Flexibility within the outsourcing contract, dispute resolution

and governance will result in strong management of the relationship and ensure a much greater success rate. The 50% of outsourcing relationships which fail are not determined by the flip of a coin, but something you can exercise control over.

Marc Dautlich, Olswang LLP: Data Protection and Security

Marc explained that the way in which to ensure good data protection and security in outsourcing is to adopt the holistic approach mentioned by Nigel. There are steps you can take before, during and after an outsourcing transaction to ensure that data is secure. For instance, proper pre-contract planning is necessary, and staff vetting and the inclusion of "accountable individual" provisions in the outsourcing contract are all different means of protecting data throughout the outsourcing lifecycle.

There are two regulatory regimes relevant to data protection and security when considering outsourcing: the FSA and the ICO. Presently the ICO does not have much weight. However, in 2010 it may be given the power to impose financial penalties based on a percentage of the company's turnover. The gap in co-operation between the two bodies is likely to close. Much of the information provided by these bodies is guidance and it can be quite difficult to turn principles-based regulation into practical security measures. That said, guidance such as the FSA's 2008 paper Data Security in Financial Services www.fsa.gov.uk/pubs/other/data_security.pdf provides practical examples and case studies. Further information is also on Olswang's blog www.datonomy.blogspot.com.

Clive Rees, Lloyds TSB: Commercial relationships – Theory v.s Practice

Clive considers that figures like Nelson Mandela, John F. Kennedy and Sir Alex Ferguson possess qualities which result in each having the capacity to manage relationships. Their shared abilities are that they can convince, listen, understand and communicate effectively, they are also emphatic and can develop trust. The relationships Financial Institutions have with suppliers are crucial to the success of the financial institution itself.

Relationships between companies are all based around expectations; too often there is a divergence of expectations which leads to a degeneration of the relationship. We are traditionally not very good at clearly articulating what we want, but the key to ensuring your expectation from a relationship is met is understanding what you want from the other party before you go to the market. Thus, create a clear tender document of what it is you actually want out of the relationship. Although price is a very important consideration, especially currently, ensure that the supplier can make a decent margin or otherwise the relationship will be unsustainable. A further key consideration is flexibility, it would be greatly beneficial if the outsourcing contract could adapt with changing circumstances. Thus, outsourcing deals should be competitive, sustainable and flexible.

Charles Kerrigan and Brian McDonnell, Olswang LLP: Industry consolidation/ regulatory considerations

Charles' main theme was the conflict between certainty and flexibility in outsourcing contracts. When a company is lending to outsourcing businesses the two key considerations are revenue and security. It is only advantageous to lend if there is a level of predictability and certainty, which is compromised if elements of flexibility are introduced. Lenders are seeking a greater amount of detail and certainty in the current economic climate, resulting in longer outsourcing contracts. A balance has to be reached between

the need for flexibility in outsourcing and the requirement of certainty from a lending standpoint. This balance has to be determined in relation to the specific function to be outsourced and considerations of whether the function is core or non-core may indeed tip the balance.

Brian explained the regulatory considerations relating to outsourcing. Regulatory considerations cannot be ignored, as the FSA is interested in all outsourcing. The approach of the FSA has altered from being seen as a "light touch" to a body that businesses should be "afraid of it". It has increased focus on large fines and is bestowing less trust on senior members of companies. He also makes the point that the Retail Distribution Review by the FSA may mean that currently existing outsourcing contracts will have to be altered to be in accordance with the Review.

Harry Taylor (moderator), Harry Taylor Consulting Ltd: Panel Discussion

Harry Taylor gave a brief summary of the main points of each of the presentations. The discussion began on the topic of regulation of outsourced functions. A company will not necessarily be less regulated merely because it has outsourced some of its functions. A company is accountable to the FSA for its outsourced suppliers and, thus, it is essential to retain a level of control over these suppliers. Companies are required to undergo extensive and intrusive due diligence procedures to ensure that they are not penalised by the FSA.

The discussion moved onto the consideration of the increase in M&A activity when a recession is ending and the impact this will have on outsourcing. Clive Rees explained that when the Lloyds Group acquired HBoS it had to spend a huge amount of time reviewing contracts HBoS had with third parties, some of which were outsourcing contracts. The Lloyds Group were required to assess whether these outsourcing contracts were effective and beneficial. M&As allow the acquiring company to weigh up the pros and cons of outsourcing and compare and contrast the companies' approach to outsourcing. However, the point was also made that when M&A occurs outsourcing contracts of the acquired company are often difficult to exit from and exiting from them will require more effort than the benefits would be worth. Many companies after M&A will concentrate on the integration of the two companies rather than a transformation.

The discussion concluded with agreement that the legal issues would depend on the form the outsourcing would take and the function to be outsourced, though good practice was attainable whatever the particular context through careful attention to the key issues raised today.

About Olswang

Olswang is a leading business law firm with a distinctive approach. Our pioneering and problem-solving ethos has established a commanding reputation in the technology, media and real estate sectors, as well as a wide range of other industries.

Founded in 1981, our Firm has grown to a team of over 650, including more than 100 partners, across four European offices. In addition, Olswang has a long-established best friends' network of leading independent law firms throughout the world.

Our Firm continues to be acknowledged as a leading practice in many of our core areas: Olswang was voted TMT Team of the Year 2009 for the second year running at the annual Legal Business Awards; Olswang's Corporate Group won M&A Law Firm of the Year at the M&A Awards 2008 in conjunction with M&A Magazine, and was named Corporate Team of the Year – Mid markets at The Lawyer Awards 2008.

Resourceful drive and a climate of shared knowledge and empowerment are the hallmarks of our meritocratic, unstuffy culture. For the last five years Olswang has been ranked in The Sunday Times 100 Best Companies to Work For and our strong management team is dedicated to the personal and professional development of our people.

We are committed to encouraging every member of staff to engage in lasting and meaningful pro bono and volunteering activities, both legal and non legal. The time invested by our people through the Firm's HELP Programme to assist those in need is a positive contribution to the community which is reflected in the values and culture of Olswang.

We recruit personalities with a genuine fascination and notable reputation in the sectors they focus on, which is reflected in the quality of our advice. We also understand the importance of achieving our clients' goals and ensure that our advice is, above all else, practical.

From world-class businesses to entrepreneurial startups, the rich diversity of our client base ensures a broader perspective and, as a result, deeper commercial insight. Transactional work is the most obvious feature of the role we perform. However, ongoing non-transactional support is an integral part of our business, and we focus on creating long-term relationships with our clients. We employ a range of proactive initiatives such as client care programmes, secondments, client training and feedback sessions to ensure our client relationships are strong.

At Olswang the passion of our lawyers, the confidence of our approach and the commercial edge to our advice provide a unique and compelling service.

OLSWANG

London
Olswang LLP
90 High Holborn
London WC1V 6XX
T +44 (0) 20 7067 3000
F +44 (0) 20 7067 3999

Thames Valley
Olswang LLP
Apex Plaza, Forbury Road
Reading RG1 1AX
T +44 (0) 20 7067 3000
F +44 (0) 20 7071 7499

Berlin
Olswang LLP
Potsdamer Platz 1
D-10785 Berlin
T +49 (0) 30 700171-100
F +49 (0) 30 700171-900

Brussels
Olswang LLP
Avenue Louise 326 bte 26
Louizalaan 326 bus 26
B-1050 Bruxelles/Brussel
T +32 2 647 4772
F +32 2 644 2165