

Developing, Preparing and Testing Plans

September 2013

David Lamb

Head of Business Resilience

FSCS

Agenda

- 1) About us
 - » What we do
 - » Why we exist
- 2) Resilience at FSCS
 - » Assessing the business needs
 - » Building appropriate plans
 - » Testing and Exercising
- 3) Testing and Exercising to date
 - » Case study
 - » Stress testing
- 4) Where does this leave us?
- 5) Q&A

Overview of the Financial Services Compensation Scheme “FSCS”

- The FSCS is the UK’s compensation fund of last resort for customers of authorised financial services firms.
- Compensation is paid when a firm is unable, or likely to be unable, to pay claims against it. This is usually because the firm has stopped trading or has been declared in default.
- FSCS was set up under the Financial Services and Markets Act 2000, and became operational in December 2001 (although we still cover claims from before this date). We are independent of the government and the financial services industry.
- Every firm authorised by the UK regulators is obliged to pay an annual levy, which goes towards FSCS’ running costs and the compensation payments made to consumers.
- Consumers are not charged for using the service and we have assisted more 4.5 million people and paid out over £26bn in compensation.
- We outsource the vast majority (95%) of our claims to third parties for processing.

FSCS's Mission

Our mission is to:

“Provide a responsive, well-understood and efficient compensation service for financial services, which raises public confidence in the industry.”

To meet this mission, we aim to:

- ❖ ***Respond quickly, efficiently and accurately to consumer claims for compensation.***
- ❖ *Raise public awareness of the protection provided by the FSCS.*
- ❖ *Ensure that FSCS operates as cost-efficiently as possible and maximises recoveries from the estates of failed providers and third parties.*
- ❖ ***Be ready to respond to defaults in the financial services industry to protect consumers and financial stability.***
- ❖ *Enhance the capability of the FSCS by enabling the people who work for us to develop their skills, knowledge and professionalism.*



Our Protection

- The FSCS covers business conducted by firms authorised by the UK regulators; the Financial Conduct Authority “FCA” and Prudential Regulation Authority “PRA” .
- European firms (authorised by their home state regulator) that operate in the UK may also be covered.
- We protect claims in relation to Deposits, Home Finance, Insurance and Investments.



FSCS before the Banking Crisis



- There was a lack of awareness of the protection in place for consumers and this resulted in the queues outside Northern Rock in September 2007; the first run on a UK bank in 150 years.
- In some cases FSCS took many weeks to process claims against failed deposit takers.
- There was no easy way to identify the final balance due to customers and therefore pay quickly.
- FSCS was therefore not a credible payout option for the sorts of firms that we were expected to resolve.

Reforms following the Banking crisis

- ❖ Following the banking crisis the deposits limit was increased to €100,000 - equivalent to £85,000 in line with Deposits Guarantee Scheme Directive (“DGSD”) limits.
- ❖ All deposit takers are required to hold a Single Customer View (“SCV”). Which is an aggregated representation of the amount of compensation due to a customer.

Faster Pay-out

- ❖ Faster pay-out enables the vast majority of customers of failed deposit takers to receive compensation within seven days, with remaining payments made within 20 days.
- ❖ The majority of claims are paid automatically, using data contained in the SCV.
- ❖ The remaining claims are processed by our third party outsourcers, with a small in-house team at FSCS providing technical support.

What does this mean?
Investment in banks’ systems and FSCS systems leads to an expectation of payout readiness that was not there before.

Resilience and planning at the FSCS

- ❖ FSCS established a dedicated Business Resilience Team in 2010. The team is responsible for ensuring that FSCS is ready for incidents and/or likely failures.
- ❖ In the past FSCS was a reactionary organisation. The aim of Business Resilience is to move FSCS to a more proactive organisation by planning/testing and exercising appropriately for all types of failure that may occur.
- ❖ **Key to this are:**
 - ❖ **Failure Modes Effects Analysis/Business Impact Assessment**
 - ❖ **Contingency/continuity plans**
 - ❖ **Testing and exercising**

Assessing the business – understand your critical activities and dependencies

Business Impact Analysis (BIA)

- ❖ Central to assessing the business is the Business Impact Analysis. This enables understanding of FSCS’s core business services, dependencies (people and technology) and appropriate timings associated with recovering our business processes.

Failure Modes Effect Analysis (FMEA)

- ❖ The FMEA tool enables us to understand the things that are likely to affect us, helping us to prioritise our testing and exercising and driving actions to control or mitigate the risks.

What failure scenario is causing concern?	What are the impacts on FSCS and consumers?	What is the severity of the effects?	What causes the impacts on FSCS and consumers?	Likelihood of failure	Current controls that prevent impacts?	Plan	People	Process	Systems	Preparedness of FSCS	RPN	RAG score	Actions for 2013/2014	Longer Term Actions	Comments



Plans

❖ To meet these aims we require two types of plan:

- **Disaster recovery plans:** plans for how FSCS will manage incidents and recover and/or restore interrupted critical (urgent) business services within a predetermined time after a disaster, failure or extended disruption. For example bad weather, systems failure or pandemics.
 - Without these we can never really be comfortable that we can perform our core functions.
- **Business contingency plans:** plans that are created to mitigate the impact of specific financial failures that FSCS might have to deal with e.g. a bank failure or life insurance failure.





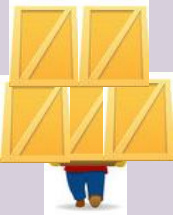


Building our plans



- To build these contingency plans we developed a standard template which contains two key sections:
 - ❖ Governance (including scope, assumptions and any document templates).
 - ❖ Mobilisation (including who is responsible and details of how to complete the step).
- The benefit of using a standard format is that everyone is familiar with the structure of the plans enabling flex across the organisation.

Testing and Exercising – needs to have a sensible mix

Type of exercise	Effort	Advantages	Disadvantages
Proof read		<ul style="list-style-type: none"> Ensures that plan makes sense and the information is correct – annual audit 	<ul style="list-style-type: none"> Doesn't engage key users of the plan
Desktop Walkthrough/Workshop		<ul style="list-style-type: none"> Easy to plan Inexpensive 	<ul style="list-style-type: none"> Doesn't necessarily test the plan in a pressure situation
Component tests		<ul style="list-style-type: none"> Able to focus on specific area of the process/plan 	<ul style="list-style-type: none"> Full end to end process not tested
Scenario test		<ul style="list-style-type: none"> Tests the end to end process Challenges assumptions and stress capability 	<ul style="list-style-type: none"> Time consuming to plan Hard to get participants to act as if it's the real thing
Full scale simulation		<ul style="list-style-type: none"> Able to engage third parties and fully exercise process/plan Creates feeling of pressure Engagement with multiple parties 	<ul style="list-style-type: none"> Expensive Time consuming to plan

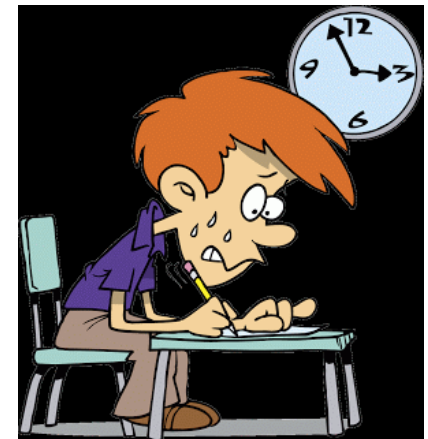
Testing and Exercising

Aims of testing and exercising:

- A systematic process to review and validate the plans to ensure operational effectiveness and meeting of requirements of the business area.
- To demonstrate that a business area can effectively respond and scale up to an incident.
- To assist with awareness, ensuring that staff are familiar with their roles and responsibilities in the event of an incident. This will reveal any shortcomings and where additional roles, documents and/or clarity will be needed.
- To test/exercise any dependent systems and third parties.

Key principles:

- ❑ Each plan tested/reviewed or used once a year.
- ❑ There must be a lessons learnt exercises following any activity.
- ❑ Testing/exercising is proportionate to the risk.



Exercising our plans - a case study

- Based around effecting a deposit payout within 7/20 days
- £9bn eligible deposits; 1 million customers
- 24 participants: Her Majesty's Treasury, Bank of England, Financial Services Authority, Insolvency Practitioners and legal participants
- Simple scenario: a bank has failed



Exercise timetable

- Contingency preparations: Pre-failure
- Escalation of contingency planning: key dependencies and timelines
- Post default processes: challenges if difficulties arise e.g. with SCV or resourcing
- Feedback sessions

Objectives and lessons learnt

Test process to enact a deposit payout

- To test ability of the authorities to work together, with a focus on exercising the adequacy of interactions between the authorities/ third parties and depositor and public communications.

Education / build relationships

- To enhance understanding and familiarity with processes, timelines, decision making and cross-authority interdependencies.

Lessons learnt

- » There were many assumptions used in contingency planning which were not based on reality.
- » Lack of clarity around roles and responsibilities and dependencies.

Stress Testing

Background:

- » IADI core principles: recommend that Deposit Guarantee Schemes (“DGS”) should carry out contingency planning and/or scenario testing.
- » Draft DGSD: peer review stress test every three years.

Objective:

- » Develop a ‘tool’ that enables EFDI members to evaluate the likely response of their domestic DGS to a range of
 - (i) common or foreseeable; and
 - (ii) extreme or unexpected adverse stress scenario

Membership

- » Broad representation from across EFDI:
 - Bulgaria
 - Czech Republic
 - Germany
 - Greece
 - Hungary
 - Italy
 - Romania
 - United Kingdom (Chair, Alex Kuczynski)
- » Range of relevant experience: live deposit payout cases and simulation exercises.



Work to date: developing the stress test framework

- » First meeting: discussed objectives, scope and timescales for work.
- » Baseline information: including underlying assumptions.
- » Lessons learnt from previous testing and exercising.
- » Scenario: range of key triggers / stress events.
- » Impact: key issues to consider.
- » Explanatory Document: tool / guide for DGS to use.



Suggested approach to conducting the stress test

- » Independent self-assessment by individual DGS (at first).
- » Consider impact channels for the scenario / case study firm.
- » Incorporate progressively more stressed inputs.
- » Method to capture the results.
- » Analysis and assessment to identify DGS' key vulnerabilities.
- » Output report, including suggested actions etc.



Where does this leave us?

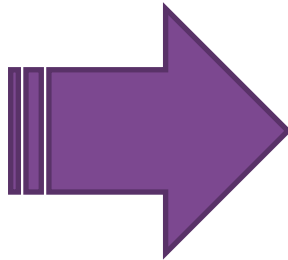
» Three lines of defence:

Operations



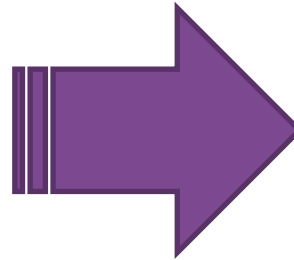
1st Line

**Contingency and
Continuity plans**



2nd Line

**Testing and
Exercising
Programme**



3rd Line



Q

&

A

T H A N K



Y O U