

EFDI Non-Binding Guidance Paper

**Operational Readiness and Resilience guidelines
for EFDI Investor Compensation Schemes**

Approved by EFDI EU Committee –28 April 2021

TABLE OF CONTENTS

SUMMARY

1. Introduction	4
2. Legal Background and Assumptions	4
3. Operational Capabilities	6
4. Operational Readiness and Resilience Planning	6
4.1 Mandate	7
4.2 Relationships With Other Safety-Net Players	8
4.3 Scalability	9
4.4 Investor Data	10
4.5 Claims Process and System	11
4.6 Security	11
4.7 Payments System	12
4.8 Funding	13
4.9 Communication with Investors and the Wider Public	14
4.10 Human Resources	15
4.11 Cross-Border Activities	16
5. Stress Testing of Operational Readiness and Resilience Plans	17
6. Conclusion	18
 Illustration of Building Blocks of an investor compensation scheme operational readiness and resilience plan.....	 19
 Appendix 1 – Issues for ICS consideration resulting from Covid 19.....	 20

Summary

- The guidelines included in this paper are intended to provide guidance to Investor Compensation Schemes (ICSs) to ensure they are ready to meet the requirements of the Investor Compensation Scheme Directive 97/9/EC (ICSD) and ensure investors receive compensation when it is due.
- This guidance is intended to help ensure ICSs are ready to be implemented when required, as well as recommending the involvement of the ICS in the wider safety-net.
- This guidance is intended to ensure that ICSs are operationally prepared to deal with a failure. ICS operational readiness and resilience plans can help contribute towards effective crisis management.

1. Introduction

1. **Directive 97/9/EC** of the European Parliament and of the Council of 3 March 1997 on investor-compensation schemes required all EU Member States to introduce an investor compensation scheme.
2. The Investor Compensation Scheme Directive (ICSD) is a minimum harmonisation directive, meaning it sets the minimum requirements for all EU investor compensation schemes (ICSs) but does not preclude Member States (MS) ICSs from providing more coverage, or a wider scope of coverage than required by the ICSD. The primary aim of the ICSD was to provide protection for investors.
3. The guidelines included in this paper are intended to provide guidance to ICSs to ensure they are ready to meet the requirements of the ICSD and ensure investors receive compensation when it is due.
4. This guidance is intended to help ensure ICSs are ready to be implemented when required, as well as recommending the involvement of the ICS in the wider safety-net.
5. Effective operational readiness and resilience planning can also contribute towards ICS crisis management plans, that is enabling the ICS to deal with a disruptive or unexpected event/s.

2. Legal Background and Assumptions

1. It is assumed that the ICS is established and has the necessary legal powers to comply with the requirements of the ICSD.
2. It is assumed all investment firms, as defined under Article 1 (2) of Directive 93/22/EEC¹ of the ICSD and authorised in accordance with Article 3 of Directive 93/22/EEC or authorized as a credit institution in accordance with Council Directive 77/780/EEC (7) and Council Directive 89/646/EEC (8), the authorization of which covers one or more of the investment services listed in Section A of the Annex to Directive 93/22/EEC, operating within the MS are required to be members of the ICS.
3. It is assumed that EEA ICSs provide investors with coverage of a minimum of €20,000 and provide coverage, as required by Article 2 for claims arising out of an investment firm's inability to:
 - *repay money owed to or belonging to investors and held on their behalf in connection with investment business,*
 - or*
 - *return to investors any instruments belonging to them and held, administered or managed on their behalf in connection with investment business,*

¹ Reference to Directive 93/22/EEC should be read as a reference to Directive 2014/65/EU (MIFID2), according to Article 94 MIFID2.

4. The guidelines for effective ICSs will cover ICS operational capabilities including payout, funding, relationship with investment firms and investors and with other members of the safety-net.

5. The ICSD provides timelines for payment of compensation by the ICS as detailed under Article 9:

1. The compensation scheme shall take appropriate measures to inform investors of the determination or ruling referred to in Article 2 (2) and, if they are to be compensated, to compensate them as soon as possible. It may fix a period during which investors shall be required to submit their claims. That period may not be less than five months from the date of the aforementioned determination or ruling or from the date on which that determination or ruling is made public.

The fact that that period has expired may not, however, be invoked by the scheme to deny cover to an investor who has been unable to assert his right to compensation in time.

2. The scheme shall be in a position to pay an investor's claim as soon as possible and at the latest within three months of the establishment of the eligibility and the amount of the claim.²

In wholly exceptional circumstances and in special cases a compensation scheme may apply to the competent authorities for an extension of the time limit. No such extension may exceed three months.....

6. It should be noted that investment firm failures can be complex and the process for establishing losses suffered, particularly if fraud has taken place, can be extensive. The three-month payout timeline may be triggered weeks or even months after the failure of the investment firm. The timeline for quantifying loss, and the overall financial position of the investment firm, is likely to be dependent on the complexity of the investigation undertaken by the relevant administrator/liquidator.

7. It should be noted that MiFID Article 14 – Membership of an authorised Investor Compensation Scheme states:

The competent authority shall verify that any entity seeking authorisation as an investment firm meets its obligations under Directive 97/9/EC at the time of authorisation.

8. It is assumed therefore that all MS investment firms comply with article 14 of MIFID II and with the 97/9/ECC Directive.

9. The single market within the EEA allows investment firms to undertake the sale and management of investments across all EEA MS. Investment firms across the EU may passport on a branch or services basis. The development of financial technology allowing the marketing and sale of investments via platforms and online marketing tools may lead to a potential increase in cross-border investment activity.

10. The ICSD, unlike the DGSD, does not contain requirements for the host state ICS to act as payout agent for the home state ICS. However, there are requirements within the ICSD, under Article 7, allowing investment firms to top-up their compensation coverage to match that of a host state ICS, if the firm operates a branch within the host state.

Article 7

1. Investor-compensation schemes introduced and officially recognized in a Member State in accordance with Article 2 (1) shall also cover investors at branches set up by investment firms in other Member States.....

....Where the level or scope, including the percentage, of the cover offered by the host Member State's investor-compensation scheme exceeds the level or scope of the cover provided in the Member State in which an investment firm is authorized, the host Member State shall ensure that there is an officially recognized scheme within its territory which a branch may join voluntarily in order to supplement the cover which its investors already enjoy by virtue of its membership of its home Member State's scheme.

If a branch joins such a scheme, that scheme shall be one that covers the category of institution to which the branch belongs or most closely corresponds in its host Member State.

Member States shall ensure that objective and generally applied conditions are established concerning branches' membership of all investor-compensation schemes. Admission shall be conditional on a branch meeting the relevant membership obligations, including in particular the payment of all contributions and other charges. Member States shall follow the guiding principles set out in Annex II in implementing this paragraph.

3. Operational Capabilities

1. EEA ICSs have varying levels of experience of dealing with investment firm failures and providing compensation to investors. The EFDI ICS WG has been developed as a way for members to exchange experience and develop best practice. This guidance is intended to form the basis for an ICS to develop the relevant capabilities to ensure, that in the event of need, the ICS is ready for implementation and able to provide effective compensation to protected investors.

2. Ensuring the ICS can effectively provide compensation to investors in the event of need will mean ICSs can effectively contribute towards consumer protection and wider financial stability.

4. Non-Binding Guidance for Operational Readiness and Resilience Planning

The guidance below is intended to provide an overview of the issues which need to be considered by all EEA ICSs for effective operational readiness and resilience planning. For the purposes of this paper **operational readiness** is defined as the capability of an ICS to efficiently deploy, operate, and maintain their systems and procedures. **Operational resilience** refers to the ability of an organisation, in this case an ICS, to identify and protect itself, as much as possible, from potential threats and possible failures, respond and adapt to, as well as recover and learn from disruptive events.

1. **To prepare an effective operational readiness and resilience plan an ICS must have a clear overview of all the steps** it will need to take to achieve payout to eligible investors of a failed financial firm.
2. If not already in place **an ICS should undertake to map its end-to-end process detailing all the processes it must undertake to successfully deal with an investment firm failure**. Each process map is likely to contain multiple steps, and the ICS may wish to break down various elements of the overall process into process maps for each step which can then be joined together to form the ICS end-to-end process. The process map should also include a detailed timeline for each step allowing the ICS to effectively plan for possible payout scenarios.
3. **Work on an end-to-end process map will allow an ICS to form an effective view of what elements need to be included in operational readiness and resilience plans and provide assurance that plans are linked directly to operational delivery**. Process maps for individual elements of the end-to-end process, such as for the claims process, or funding requirements, will also provide the opportunity for the ICS to build operational readiness and resilience plans for each block of the overall process.
4. **End-to-end process mapping, and its inclusion in operational readiness and resilience plans, will allow the ICS to test elements of the process** as well as the entire end-to-end process. Testing of operational readiness and resilience plans are vital.
5. **ICS operational readiness and resilience planning must be subject to ongoing review and revision**. Changes and improvements may be driven by amendments to relevant regulation and legislation, decisions of the Courts within the relevant MS, and from lessons learned after completion of live resolution and payout cases.

4.1 Mandate

ICSs across the EEA have varying mandates involving differing roles and responsibilities. For example, in the UK the FSCS has responsibility for negligence and mis-selling claims as well as non-return of investment assets and monies. This means FSCS must be ready to deal with both types of claim. ICSs may have responsibility for resolution as well as payout and may also have powers to act as administrator and/or liquidator of the failed investment firm.

6. **If the ICS has powers to act as liquidator/administrator they should ensure that they have the capability to fulfil this element of their mandate.** This may involve ensuring they have staff with the relevant skill set to enable the ICS to act as liquidator/administrator either permanently employed or have arrangements in place to access staff with the relevant capabilities. This could be via a contractual arrangement ensuring the required staff resource is available when needed. Such contractual arrangements should be considered in advance as part of operational readiness and resilience planning to ensure staff with the relevant skill sets can be called upon promptly to ensure effective delivery of the ICS mandate.
7. **If the ICS does not have liquidator/administrator powers then it is likely they will need to work with a liquidator/administrator,** who may be appointed by the relevant regulatory or legal authorities. If this is the case the ICS should consider in advance, as part of their operational readiness and resilience plans, the information the ICS will require to enable them to effectively deliver compensation promptly to eligible investors. The information exchange between the ICS and the liquidator / administrator, appointed by the Courts and/or regulatory authority, should be guided by relevant legislation and or rules and guidelines already in place for insolvency of investment firms.
8. For best practice where possible, **the ICS should consider developing relationships with those bodies which are responsible for liquidation and/or administration of failed investment firms.** Such relationship development would allow the ICS to agree, in advance of any failure, the information the ICS would need, and the timelines for delivery of the information, to enable payment of compensation to eligible investors.
9. The ICS may want **to consider developing guidelines detailing the information required by the ICS for payout, which can be shared with the relevant bodies and regulatory authorities to ensure all parties are aware of the needs of the ICS to effectively deliver its mandate.** This sharing of information would allow the ICS to engage in effective planning and ensure all parties involved in a potential failure are aware of the ICS requirements prior to any failure taking place.
10. Such requirements and **pre-planning would also allow the ICS to identify whether the process in place** within its MS, which governs the liquidation and/or administration of a failed investment firm, **is fit for the purposes of the ICS.** If gaps or issues are identified during ICS operational readiness and resilience planning, they can be communicated to the relevant bodies and discussions can be initiated about possible changes. ICS operational readiness and resilience planning for liquidation and/or administration will allow the ICS to highlight issues or concerns, or gaps in the regulatory or legal process which could hinder the effective delivery of ICS compensation, prior to any failure.
11. **Effective ICS** operational readiness and resilience **planning will also serve** to develop **confidence amongst other participants in the financial safety-net** as to the ability of the ICS to deliver its mandate.

4.2 Relationships with Other Safety-Net Players

12. The mandate and governance structure of the ICS may impact upon its role within the financial safety-net. Regardless of this **all ICSs should be involved with other safety-net**

players, in particular the regulatory authorities responsible for the supervision of protected investment firms. Exchanges of information within the safety-net as to overall market conditions, and information relating to specific firms, is desirable in order that an ICS can effectively plan for failure. For an ICS to be effective it must have confidence that where possible it will be provided with notice of an impending investment firm failure. Awareness of a potential failure/s will allow the ICS to trigger its operational readiness and resilience plans and prepare to deal with investors. Consideration should be given to formalising the relationship between the ICS and other safety-net participants, and information exchange requirements, via a Memorandum of Understanding or Protocol.

13. **If resolution tools for investment firms exist** in the MS, regardless of whether they sit with the ICS or another resolution body, **the ICS should be involved.** Step-by-step planning of resolution options may well need to include payout as a possible last resort option.

14. It should be stressed to all safety-net participants that **keeping the ICS in the information loop about possible market or firm failures means the ICS is better prepared when triggered. A well-prepared ICS able to effectively fulfil its mandate will be able to deliver its contribution to consumer confidence and financial stability.** Involvement of the ICS during peacetime allows effective preparation to be undertaken. The development of relationships between the financial safety-net participants, including the ICS, is also an added benefit, as these relationships will be called upon if an investment firm fails and the ICS is called upon to deliver compensation.

15. **Involvement of other safety-net participants as part of ICS operational readiness and resilience planning will also demonstrate ICS capability and provide confidence** to the other parties within the financial safety-net that the ICS is fit for purpose.

16. **Development of an effective, detailed operational readiness and resilience plan by the ICS, and testing of that plan, will enable the ICS to identify where they may need specific assistance from supervisory/regulatory authorities.** The ICS can then enter discussions about the specific assistance and/or information required to enable the ICS to effectively deliver its mandate, be that resolution and/or payout.

4.3 Scalability

17. To effectively prepare for potential investment firm failure/s **the ICS should engage with the relevant regulatory authorities as to the expectations regarding the capability of the ICS. The ICS and its partners within the financial safety-net should have an awareness of the investment market within its own MS.** Regulatory information as to the size of the investment markets and firms operating within the market should be available to the ICS. The information required by the ICS may not include market sensitive or confidential information but, to allow for effective operational readiness and resilience planning, a conversation is required amongst participants within the financial safety-net as to the tools available for dealing with investment firm failures, including the triggering of the ICS.

18. **The ICS will require some guidance and assurances as to the likely scale of any potential failure in order that the ICS can undertake effective operational readiness and**

resilience planning. If there are resolution tools for investment firms in place in the relevant MS, the ICS and other members of the financial safety-net should discuss the investment firms for whom resolution and not payout is the preferred option. For those investment firms for whom resolution is not the preferred option it is assumed that payout via the ICS is the default option.

19. **To prepare effective operational readiness and resilience plans ICSs will need to understand the likely maximum size of investment firm failure the ICS would be expected to prepare for.** It is only with information as to the possible scale and scope of potential firm failures that an ICS can effectively build operational readiness and resilience plans and have confidence in its ability to deliver its mandate.

20. **ICS operational readiness and resilience plans should also take account of the possibility of multiple investment firm failures** occurring at the same time, or over a short period of time, such as during a systemic crisis.

4.4 Investor Data

21. In the event of failure of an investment firm who has customers who may be protected by the relevant MS ICS the **ICS must have the capability to receive the relevant consumer data.**

22. The ICS must consider what investor information and information it requires to pay compensation. **The ICS should develop a standardised data requirement covering the elements required to enable the ICS to assess and pay investment claims.**

23. **The information required will include as a minimum:**

- I. Name and contact details for the investor
- II. Type of investment
- III. The original investment amount and amount now recorded as the investment balance in failed investment firm records
- IV. The ICS may require other information such as the details of the relevant investment products provided by the failed firm. The ICS may also require the failed investment records for each individual investor which would record the dates and amounts of the original investments and subsequent payments and withdrawals on the investors account/s.

24. The ICS will need to consider exactly what information is required to assess the investors claim for compensation and the information it requires to complete the claim process and complete a payout. If the compensation limit applies on an individual aggregated basis consideration must be given to information about joint accounts and client assets, and the information the ICS will need in respect of these accounts. **The ICS will need to be able to share the list of data required with the relevant liquidator and/or administrator at the time of failure.** It is also recommended that the information required should be shared with the relevant regulatory bodies to ensure all parties in the financial safety-net are aware of the information the ICS requires to enable it to deliver payout.

25. If the jurisdiction requires regulated investment firms **to hold investor data in a specific format it is recommended that the regulatory authorities and the ICS engage in discussions to ensure the investor data format includes all necessary information required** by the ICS and/or the Resolution Authority (if applicable).
26. **If the ICS has a mandate including powers to make onsite visits** to protected investment firms, it may wish to **assess investor data when onsite**. If onsite data assessment is part of the role and responsibilities of the ICS then the results of such assessment, and the **sharing of this information** within the financial safety-net, will need **to be considered as part of broader ICS operational readiness and resilience planning**.
27. As part of the ongoing ICS operational readiness and resilience planning process **the investor information required** for an effective payout **should be reviewed on a continuous basis**, and particularly following any payout events following a lesson learned process.

4.5 Claims Process and System

28. To undertake a payout **an ICS will need a system enabling it to process investor claims for compensation**. The ICS claim system requirements will vary between ICSs as there are no requirements detailed within the ICSD, or guidelines issued by an external body.
29. **An ICS will need to consider its role and responsibilities to ensure any claims system works for the benefit of the ICS, as well as investors** who may need to use the system in the event of an investment firm failure.
30. To develop an effective investor claim system, **the ICS will need to have developed an end-to-end claims process**. An end-to-end claims process will allow the ICS to work through and identify all the elements needed to deliver investor payout.
31. **An effective end-to-end process should consider all processes needed to** (the order of the relevant steps may vary depending on the ICS):
- I. receive the relevant investor information and data from the failed investment firm or the liquidator and/ or administrator;
 - II. if required by the ICS rules, receive a claim from the investor;
 - III. assess and verify the eligibility of the investor;
 - IV. assess and verify the loss suffered by the investor;
 - V. apply the ICS compensation limit; and
 - VI. make payment to the investor.
32. When the ICS has completed its end-to-end process planning it will **need to consider the resources required to deliver the end-to-end process**. The resources will include an effective IT or information system, human resources and sufficient funding needed to deliver both the resources required and compensation payments.
33. **Any effective claims process and system must be scalable**. As discussed previously in this paper the likely maximum scale of any investment firm failure is an important factor for delivery of an effective ICS. Any claims system must also take account of the possibility of multiple failures and ensure systems, processes and resources can respond to the scale required.

34. As with all elements of operational readiness and resilience planning **the claims process and systems will need to be reviewed following stress testing or payout.** Testing of the claims process and systems will allow the ICS to continually assess process and system effectiveness and make changes and improvements when identified.

35. An effective end-to-end process **should also take account of the involvement of third parties including regulatory authorities.** Any participation of external third parties in the end-to-end process and claims system should also be tested as part of the ICS operational readiness and resilience plans.

4.6 Security

36. **The ICS claims system will need to be able to record all information necessary for the assessment of claims including personal investor information.** As personal investor information is retained by the ICS for the purposes of its mandate the ICS **must take the necessary steps to ensure security of investor data** and comply with the requirements of GDPR and/or national data security requirements.

37. **ICS's should also consider their overall Information security management (ISM).** ISM describes controls that an organisation needs to implement to ensure that it is sensibly protecting the confidentiality, availability, and integrity of its assets from threats and vulnerabilities. As part of information security management, an organisation may implement an information security management system.

38. **ICS operational readiness and resilience plans should include consideration of the effectiveness of ICS data security and their information security management.** An ICS should give consideration to developing a holistic Business Continuity Process (BCP) as part of the Information Security Management System.

4.7 Payments System

39. The result of the ICS claims process should enable the ICS to make payment of compensation to eligible investors. **The ICS must have appropriate payments system or systems enabling payment to be made in place and ensure payments systems are an integral part of operational readiness and resilience planning.**

40. The ICS will need to ensure that **a process has been developed which will enable the ICS to undertake an assessment of the relevant investment firm records to assess potential losses.** Any such process may require accountancy or legal specialists, either permanently employed by the ICS, or available via an outsourced or contractual arrangement.

41. If the ICS is reliant on the liquidator and/or administrator for access to investor records they may also be reliant on the liquidator and/or administrator to establish an accurate picture of the investment firm losses and individual investor balances. If this is the case the **ICS will need to work closely with the relevant liquidator and/or administrator to ensure access to information.** In such cases timelines for establishing claims may be subject to the control of the liquidator and/or administrator.

42. **The ICS payments system should take account of the possible scale of any payout and ensure any payments system can deliver the scale of payments required.**

43. **Any testing of the ICS operational readiness and resilience plans should include the testing of the payments system, including third-party providers** at some point during the operational readiness and resilience plan testing cycle.

44. Payments of investor compensation may take place over an extended period, depending on the type of investment firm failure involved and the scale of investor losses, and planning for **an extended timeline** is something **to be considered when preparing operational readiness and resilience plans.**

4.8 Funding

45. **An ICS must have access to sufficient funding to enable it to deliver compensation to investors** when called upon. The funding may come from a variety of sources, depending on the ICS model, which may include:

- I. Ex-ante funding – managed by the ICS or a third-party
- II. Ex-post or extra-ordinary contributions from ICS levy payers
- III. Commercial funding arrangements - this may include credit facilities including overdraft and loan arrangements, insurance policies, possible debt issuance by the ICS or a third party.
- IV. Back-up funding from the Central Bank or MS Government

46. **The key issue for the ICS when triggered is the ability to access sufficient funds when needed.** Unlike a deposit failure the funds to cover an investment firm failure may be required over a longer timeline, and multiple drawdowns may be required as claims are paid over an extended period

47. **As part of ICS operational readiness and resilience planning the ICS should consider the individual elements of its funding model and how this may impact its planning.** The size of any ex-ante fund and the liquidity of those funds, or the ability of its member firms to pay extraordinary contributions, potentially during a systemic crisis, are all factors which may influence the ICS operational readiness and resilience funding plan. If back-up funding were required for a failure of a certain size, formal arrangements should exist detailing the accessibility of the back-up funds and the likely terms and conditions for accessing such funds by the ICS.

48. As part of ICS operational readiness and resilience planning **the ICS will need to consider various scenarios and how such scenarios would be funded, which may involve a range of funding options.** The ICS should consider formalising any arrangements involving potential third-party funding to ensure the relevant funds can be called upon by the ICS as and when required. Security and risk-profile for ICS fund investment will also need to be considered, particularly if the ICS engages a third-party to manage funds. ICS investment strategy, in particular liquidity of the ex-ante fund and access to funds, will also need to be considered when making assumptions for access to the fund as part of ICS operational readiness and resilience planning.

49. Regardless of the ICS funding model it will be vital that all possible funding scenarios are considered as part of operational readiness and resilience planning. As part of ongoing testing of the operational readiness and resilience plans it will be important that the ICS tests its ability to access liquid funds and this may require the involvement of third parties, such as commercial banks or the Central Bank and/or the Ministry of Finance.

50. **To effectively contribute to consumer confidence and financial stability it is vital that the ICS has plans in place to fund any potential investment firm payout.** This element of operational readiness and resilience planning highlights the need for the ICS to enter serious discussions within the financial safety net at the possible size and scale and cost of any potential investment firm payout.

4.9 Communication with Investors and the Wider Public

51. **As part of ICS operational readiness and resilience plans it is vitally important that consideration is given to communication plans for engaging investors before and during a failure.** Effective operational readiness and resilience plans should include communication plans built in peace time to make investors aware of the existence of the ICS. An awareness of the ICS provides better confidence in the financial system and facilitates the compensation process thanks to better prepared investors. Building awareness during peace time is likely to require the support of the other members of the financial safety-net and may involve industry participants and engagement with opinion formers who may be supportive during a payout or crisis event. Effective operational readiness and resilience plans should include communications from the date of failure and continued ongoing communication with investors during, and potentially after, the claims process.

52. **Pre-preparation will ensure that on day one the ICS is ready to communicate reassuring messages about the role and responsibilities of the ICS.** Depending on the role of third-parties in the insolvency and/or administration process, such as lawyers or accountants, it would be good practice, as part of operational readiness and resilience planning, to understand exactly what messages are likely to be shared with investors as part of the investment firm failure process.

53. **The ICS will need to also understand the roles and responsibilities, regarding communications with investors and the wider public, of the other members of the safety-net.** Development of a shared message within the financial safety-net ensuring consistent messaging to investors and the wider public will help reinforce the ICS message to investors.

54. It should be noted, as stated earlier in this paper, **the triggering for payout by the ICS may take place weeks or months after the firm's failure**, depending on the reasons for, and the complexity of, the investment firm failure. **Communication plans by all members of the safety-net, including the ICS, will need to undertake careful messaging during this period** to ensure consumers, and other stakeholders including politicians, press and levy payers, understand the reasons for the delay between investment firm failure and ICS payout. **Perceived delays in payout must not contribute to any damage to the reputation of the ICS and consumer confidence.** ICS communications operational readiness and resilience plans must take this possible delay factor into account.

55. **The ICS will need to consider all elements of the communication process and the tools to be used.** The ICS operational readiness and resilience plans should contain communications templates detailing the core information that would need to be communicated to investors with any failed investment firm. It is acknowledged that templates are likely to need adapting for individual firm failure circumstances. The ICS operational readiness and resilience plan will need to consider the communication resources, including human resources, which will need to be in place at the point of failure.

56. **Operational readiness and resilience planning will need to consider the potential scale and scope of any failure and which tools the ICS will need to use in the event of an investment firm failure.** These tools may include:

- I. ICS website include messaging and Question & Answers' (Q&A's)
- II. Letters to investors
- III. Telephony Q&A's
- IV. Public relations with newspapers, radio and/or TV
- V. Social Media

57. **A comprehensive operational readiness and resilience plan for communications should identify the resources required.** It is acknowledged that ICSs may not have the specialist communications resources required as part of their business as usual resources and external assistance may be required. The EFDI PR and Communications Committee may be able to assist as they have developed templates for deposit failures which could be adapted by ICSs. The EFDI PR and Communications Committee may also be available to provide guidance on the elements required for an effective communications plan.

58. It is important to note that **communications during a payout event are likely to be ongoing to ensure investors and the wider public are kept up to date as to the progress of the payout.** Operational readiness and resilience plans must take account of this ongoing communications need and potential resource implications.

59. **Once the ICS has developed an effective communications contingency plan it should be able to start a discussion with the other members of the financial safety-net as to any gaps and issues identified.** The ICS will also be able to contribute to a broader financial safety-net plan where roles and responsibilities for communications during an investment firm failure are clearly understood by all the involved parties.

60. As with all other elements of the ICS operational readiness and resilience plan **ongoing testing of the communications operational readiness and resilience plan will be required.**

4.10 Human Resources

61. The EEA ICS community has widely varying levels of experience with some EEA ICSs never having been triggered. **ICS operational readiness and resilience plans must therefore consider where staff resources will be obtained from in the event of an investment firm failure requiring ICS payout.**

62. **The human resources needed by the ICS to deliver its mandate effectively should be identified during the mapping of the end-to-end claims process** mentioned previously. The

end-to-end claims process map will allow the ICS to identify the roles and responsibilities for which additional resource may be needed. Once the roles and responsibilities are identified as part of the ICS operational readiness and resilience plans the ICS can then plan how best to resource the additional resources required.

63. **An ICS may well require staff with specialist skills, both during business as usual times and particularly during a payout case.** This may include skills such as operational implementation, risk management, understanding of funding and finance, as well as awareness and understanding of the MS investment market and products. Depending on the size of the ICS these skills may be based inhouse, or accessible via an outsourced or consultancy basis.

64. The ICS may have contractual arrangements in place with third-party providers such as accountants, legal firms, telephony staff providers, payout providers etc. If this is the case, **as part of ICS operational readiness and resilience plans, the retention and implementation of arrangements for third party providers should be detailed and tested as part of the wider stress-testing program.**

65. **If ICS resource operational readiness and resilience plans include staff resources from regulatory bodies the requirements of the ICS would need to be agreed** as part of a wider conversation with all members of the financial safety-net.

4.11 Cross-Border Activities

66. **ICSs should be aware if any investment firms based within another EEA state have topped-up into their ICS in relation to level and/or scope of coverage.** If an investment firm has topped-up, the **home and host state ICS should cooperate to support an effective additional payout process by the host state ICS so that** the roles and responsibilities of both the home and host state ICS are sufficiently clear and detailed, and so they could check how this cooperation **would work in practice.**

67. **There are a broad range of issues relevant to cross-border investment activities which need to be considered as part of broader home state ICS operational readiness and resilience plans.**

68. **For non-resident investors and investors with a branch of an investment firm in another EEA state the ICS will need to consider communication,** and whether there are sufficient investors in another MS to require specific messaging, for example with the website containing messages and Q&A's in multiple languages.

69. **Payment options may also need to take account of cross-border activity.** For example, an agent bank arrangement in a scenario involving multiple investors based outside the MS may not be suitable, and alternative payment measures may need to be considered. The ICS operational readiness and resilience plans should at the least consider the possibility of dealing with investors based outside the home state and what impact this could have in the event of a payout.

70. **Information as to the exposure of home state investment firms in other MS should be a discussion point between the relevant regulatory authorities and the ICS.** Information as

to the scale of home state investment firms cross-border activity, and where such activity is located, should be a contributing factor for ICS operational readiness and resilience planning

71. **For a branch based in another MS the home state ICS may consider entering into bilateral agreements with the host state ICS.** This bilateral agreement could be complex but might allow the home and host state ICSs to discuss possible assistance which could be provided by the host state ICS in the event of failure, including assistance with communication plans. Ongoing home-host cooperation and testing of bilateral arrangements will need to be part of any stress-testing of the ICS operational readiness and resilience plans.

72. As part of its ongoing discussions with other members of the financial safety-net **the issue of branch business or investors based in another MS should be a factor for consideration when discussing the potential failure of any investment firm.** The ICS should make its financial safety-net partners aware of the possible complexities such a scenario may add to a payout. Developing an ICS operational readiness and resilience plan identifying these possible complexities will allow all members of the financial safety-net to fully understand the possible consequences of a cross-border failure for the home state ICS.

73. **ICSs which have members engaging in cross-border branch investment will need to consider cross-border activities and engagement with host state ICSs** as part of their broader operational readiness and resilience plans. As with all ICS operational readiness and resilience plans there will need to be a testing cycle in place and both parties to any bilateral agreement will need to be involved.

5. Stress Testing of Operational Readiness and Resilience Plans

1. **Stress Testing of operational readiness and resilience plans is undertaken to provide reassurance that the ICS systems would work when required.** In this scenario the system involves the ICS operational readiness and resilience plan, which requires testing to ensure ICS capability and preparedness for a payout or crisis scenario.

2. Unlike the DGSD the **ICSD sets no requirements for operational readiness and resilience planning or stress-testing of ICS capabilities but it is recommended both are put in place.** It is acknowledged that it may not be necessary to undertake a full end-to-end stress test for all elements of the ICS operational readiness and resilience plan on an annual basis, however **an annual test of at least one or more elements of the ICS operational readiness and resilience plan could be considered.** This could involve, for example, testing funding capabilities, communication plans, claims system testing etc.

3. To ensure the ICS has full confidence in its ability to deal with an investment failure or failures it **could consider testing the full operational readiness and resilience plan from end-to-end at least every three to five years.** Stress-testing of all, or part of the ICS operational readiness and resilience plans, provides reassurance as to the ICS ability to undertake a payout. Stress-testing the operational readiness and resilience plans also allows the ICS to identify gaps or issues with its systems or processes. Following the stress-test the ICS can work to resolve those gaps or issues identified.

4. **The ICS should involve**, where possible, **other members of the financial-safety in elements of the stress-test program where applicable**. For example, testing of the funding capability could involve the Central Bank and/or the Ministry of Finance if back-up funding is part of their remit and interaction with the ICS.
5. **A robust stress-testing program provides confidence in the ability of the ICS to fulfil its mandate to the Executives and Board of the ICS**. The stress-testing program can also provide reassurance to other members of the financial safety-net as to the ability of the ICS to undertake a payout.
6. **Stress-testing of the ICS operational readiness and resilience plans will also lead to lessons learned** which can be shared with the Board of the ICS and other members of the financial safety-net, if applicable. Issues and gaps identified may, in some cases, only be resolvable via third party assistance, such as changes to legislation or rules, whilst others may simply require changes to ICS systems and processes.

6. Conclusion

1. This guidance has been developed to aid the development of effective operational readiness and resilience plans by EFDI ICS WG members. It is a high-level document providing guidance as to the issues to be considered as part of operational readiness and resilience planning. It is acknowledged that some ICS may require additional resource to develop operational readiness and resilience plans, and a stress-test programme, but this document is intended to serve as a useful first step in the process.
2. The EFDI ICS WG intends to undertake further work in relation to ICS operational readiness and resilience planning and stress-testing. It is also planned for the EFDI ICS WG to take advantage of the expertise available within the EFDI through joint work with the Communications and PR Committee and the Stress-Test WG.
3. This paper was originally authored prior to Covid-19 and considering the potential wide-ranging consequences of Covid-19 an appendix has been added to this paper detailing other issues which ICSs may wish to consider. What has been highlighted by Covid-19 is the need for ICSs to have effective operational readiness and resilience plans to ensure they are ready always to deal with investment firm failures and deliver their role in consumer protection and contribution to financial stability.

Author – Karen Gibbons, Head of International Liaison and Research – FSCS, UK

January 2021.

Building blocks of an investor compensation scheme operational readiness and resilience plan



Appendix 1 – Issues for ICS consideration resulting from Covid 19

1. The Covid-19 pandemic demonstrated the need for all firms, including investor compensation schemes, **to have effective disaster recovery and business continuity plans in place**. This paper does not refer to the requirements for an ICS to have effective plans to deal with an event such as Covid-19 but it may be helpful for an ICS to consider the following elements for future reference, and when considering plans for business continuity and disaster recovery.

- I. **Business continuity planning (BCP)** is the process involved in creating a system of prevention and recovery from potential threats to a company. The plan ensures that personnel and assets are protected and can function quickly in the event of a disaster. The BCP is generally conceived in advance and involves input from key stakeholders and personnel. BCP involves defining all risks that can affect the company's operations, making it an important part of the organisation's risk management strategy. Risks may include natural disasters and pandemics.
- II. A **disaster recovery plan (DRP)** is defined as a documented, structured approach that describes how an organisation can quickly resume work after an unplanned incident. It usually refers to the aspects of an organisation that depend on a functioning IT infrastructure.

2. **All ICSs should have an effective risk and resilience framework in place including effective business continuity and disaster recovery plans.** Covid-19 has identified why this planning is so important and highlighted issues which ICSs should consider as part of their forward planning, including issues such as remote working. During the Covid-19 crisis many organisations, including ICSs, have only been able to continue working by enabling their staff to work remotely. Organisations which have been able to implement an effective home working plan have been able to do so because of successful business continuity planning.

3. When building an effective ICS operational readiness and resilience plan, it is now likely, as a result of Covid-19, that the ICS will need to consider how they would be able to deal with a failure occurring whilst they are working remotely, or for some reason access to their office, or some or all systems, are not available. This work can either be considered as part of the broader operational readiness and resilience or separately as part of the business continuity or disaster recovery plans. It is important that the ICS coordinates its operational readiness and resilience, business continuity and disaster recovery plans to ensure they can all be effectively delivered.

4. Covid-19 is also likely to have longer term impacts on the general economic situation. The potential scale and scope of that impact will be highly dependent on the length of the initial lockdown and whether or not we see a third wave of global infection. Any economic downturn may also have longer term impacts on investment firms, and financial markets more generally, and will highlight the need for ICS involvement in the financial safety net. Ongoing regular discussions with regulatory authorities and industry representatives will help ICSs effectively prepare for future failures.