

Guidance Consultation

GC16/5 - Proposed guidance on wind-down planning

May 2016

1 Introduction

- 1.1 The FCA proposes to issue a guidance document entitled 'The FCA's approach to wind-down planning' (the 'approach document'). The draft approach document can be found in Annex 2 to this Consultation.
- 1.2 In wind-down planning, a firm considers how it could close down its regulated business in an orderly manner, including under stressed conditions.
- 1.3 This approach document offers an approach to wind-down planning to assist any solo-regulated firms that may need to wind-down. It is not a prescribed approach and firms can depart from it as they choose or use completely different approaches. The approach document does not by itself impose any obligations on firms to create wind-down plans. The intention of this approach document is to make some helpful suggestions in order to assist firms' thinking in this context.
- 1.4 This Consultation is aimed at FCA solo-regulated firms, especially those which currently perform related analyses, e.g. estimating wind-down costs for capital planning.

2 Summary of the approach document

- 2.1 Authorised persons and professional advisors have requested that the FCA provides clarification on what wind-down planning should cover. To date, we have discussed wind-down planning with individual firms as part of our supervisory response to identified concerns. In May 2015 we provided feedback to the wider industry as part of our Prudential Forum. In addition we believe that this non-binding approach document will benefit firms and their professional advisors and lead to better outcomes.
- 2.2 The proposed approach document, when finalised, will become general guidance in the FCA Handbook under the 'Regulatory Guides' section.
- 2.3 The approach document itself does not impose an obligation on firms to create wind-down plans, but merely suggests a logical approach for firms that have decided to engage in such planning. As such, it is not being subjected to cost-benefit analysis. We accept that there are many different approaches to wind-down planning, so we encourage firms to take this approach document into consideration as a starting point and tailor a model that best suits their circumstances.
- 2.4 The approach document's main body has two parts: Chapter 3 discusses the concept and process of wind-down planning and Chapter 4 discusses some more specialised topics, e.g. communications plans. The approach document is accompanied by a Quick Reference Guide which may be particularly useful for smaller firms.
- 2.5 We believe that an effective wind-down plan should help a failing firm to cease its regulated activities and achieve cancellation of permission with minimal adverse impact on its clients, counterparties and the wider markets. So the approach document aims to help a firm factor these considerations into its wind-down planning.
- 2.6 In simple terms, wind-down planning is a process by which the governing body of a firm:
 - identifies the steps and resources it needs to wind down its business, especially in a resource-stressed situation, and
 - evaluates the potential risks and impact of a wind-down and considers how to mitigate them.
- 2.7 The approach document places emphasis on the leadership of the firm's governing body in its wind-down planning.
- 2.8 The cases we have seen recently show that a significant number of firm failures are caused by stressed financial, operational or other events, including sudden market changes. Given this, key pre-requisites for an orderly wind-down include the ability to monitor relevant indicators and make effective and timely decisions. Effective wind-down planning is therefore likely to be enhanced by an effective risk management framework.

2.9 We believe there are three important assessments that a firm is likely to include as part of effective wind-down planning:

- Impact assessment: Who will be affected by the wind down if it happens?
- Operational analysis: What steps would need to be taken during the wind-down process?
- Resource assessment: What resources would be needed to complete the steps identified in the operational analysis?

2.10 Amongst the several special topics in Chapter 4, we have noted that there are two areas in particular that many firms have tended to overlook:

- A communications plan
An effective communications plan can help to deliver a more effective wind-down process and ensure appropriate and timely action from all key stakeholders.
- Assessment of intra-group relationships (where relevant)
If a firm is part of a larger group, its wind-down plan will often be affected by the availability or the withdrawal of group financial support, processing capabilities and shared staff and facilities. If the entity has been relying on support and services from the wider group, then it is prudent to consider if these resources would still be available during the wind-down.

2.11 The Quick Reference Guide gives some helpful hints on how to put the theory into practice, as well as some examples as illustration.

3 Next steps

3.1 We would welcome any comments or observations by 22 July 2016 (Friday). Following that, and taking into account any responses received, we will look to issue a final statement of our guidance on this matter.

3.2 Responses may be sent in writing to the following address:

F.A.O. Anthony Ma / Gerald Sampson
Specialist Supervision Division
The Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Email: WDP-feedback@fca.org.uk

Annex 1: Compatibility statement

Compatibility statement

1. Section 1B of the Financial Services and Markets Act 2000 (FSMA) requires the FCA, when discharging its general functions, as far as is reasonably possible, to act in a way that is compatible with its strategic objective and advances one or more of its operational objectives. The FCA also needs to, so as far as is compatible with acting in a way that advances the consumer protection objective or the integrity objective, carry out its general functions in a way that promotes effective competition in the interests of consumers. The FCA's general functions include its functions in relation to the giving of general guidance.
2. The FCA believes the proposals set out in this Consultation are compatible with its duties under section 1B of FSMA. Guidance for wind-down planning will help firms to consider how an orderly wind down can be achieved and how to make such decision in a timely manner. It also helps firms to appreciate how the winding down will affect various stakeholders (including consumers and market participants). This in turn advances our objectives of protecting consumers' interests and market integrity.
3. The FCA has had regard to the regulatory principles set out in section 3B of FSMA. In formulating the proposal, the FCA adhered to the principle of proportionality. A suggested approach to wind-down planning contributes to better regulatory outcome, whilst not imposing significant (if any) burden on firms. The proposals are also consistent with the principle that the FCA should exercise its functions as transparently as possible

Cost benefit analysis

4. The proposal set out in this Consultation does not impose additional obligation on firms. It is not related to rule changes or guidance on rules. Under section 138I of FSMA, when the FCA wishes to introduce any new rules it must publish a cost benefit analysis (CBA) along with the proposed rules. Since the requirements under section 138I are not applicable, the FCA is not required to carry out a CBA. In any event, the FCA does not expect that the proposal will lead to any increase in costs, or the cost increase will be of minimal significance.

Equality and diversity

5. We have considered the equality and diversity issues that may arise from these proposals. Overall, we do not consider that the proposals raise concerns with regard to equality and diversity issues.
6. We do not consider that the proposals in this Consultation adversely impact any of the groups with protected characteristics, i.e., age, disability, sex, marriage or civil

partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment.

7. We will continue to consider the equality and diversity implications of the proposals during the consultation period, and will revisit them when publishing the final guidance. In the interim we welcome any feedback to this Consultation on such matters.

Annex 2: The FCA's approach to wind-down planning (including Quick Reference Guide)

WIND-DOWN PLANNING GUIDE INSTRUMENT 2016

Powers exercised

- A. The Financial Conduct Authority makes this instrument in the exercise of its powers under section 139A (Guidance) of the Financial Services and Markets Act 2000.

Commencement

- B. This instrument comes into force on [*date*].

New regulatory guide

- C. The Financial Conduct Authority makes the ‘Wind-down Planning Guide’ to form a Regulatory Guide in accordance with Annex A to this instrument. The Regulatory Guide does not form part of the Handbook.

Notes

- D. In the Annex to this instrument, the “notes” (indicated by “**Note:**”) are included for the convenience of readers but do not form part of the legislative text.

Citation

- E. This instrument may be cited as the Wind-down Planning Guide Instrument 2016.
- F. The sourcebook in Annex A to this instrument may be cited as the Wind-down Planning Guide (WDPG).

By order of the Board
[*date*] 2016

Annex A to Wind-down Planning Guide Instrument 2016 Wind-down Planning Guide (WDPG)

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1 Introduction

1.1 Overview

- 1.1.1 An effective wind-down plan aims to enable a *firm* to cease its *regulated activities* and achieve cancellation of its *permission* with minimal adverse impact on its *clients*, *counterparties* or the wider markets. This includes scenarios where the *firm* undertakes a strategic exit as well as unexpected crisis or insolvency that makes the *firm* unviable.
- 1.1.2 A wind-down plan can also help a *firm* to assess if it would have adequate resources (e.g. capital, liquidity, knowhow and manpower) to wind down in an orderly manner, especially under challenging circumstances.
- 1.1.3 The Quick Reference Guide at the end of this approach document is intended to help *firms* (especially those of a smaller size or a simpler operating model) to apply the theory to develop an effective wind-down plan.

2 Application and interpretation

2.1 Application and interpretation

- 2.1.1 This approach document aims to assist any solo-regulated *firm* that undertakes wind-down planning. It does not apply to any *PRA-authorised person*. It does not impose any obligation on a *firm* to create a wind-down plan. However, it shows what an effective

wind-down plan can include, for *firms* that choose to have one to demonstrate how this can assist meeting its general obligations.

- 2.1.2 This approach document is general *guidance* given under section 139A of the Financial Services and Markets Act 2000 (the 'Act').
- 2.1.3 Interpretative provisions (including definitions in the *Glossary*) of the *FCA Handbook* apply to this approach document in the same way they apply to the *FCA Handbook*. Where a definition is defined in the *Act*, that definition applies in this approach document.

3 The concept and process of wind-down planning

3.1 What is wind-down planning?

- 3.1.1 Wind-down planning is a process in which the *firm's governing body*:
 - (1) identifies the steps and resources it needs to wind down its business, especially in a situation where resources are limited; and
 - (2) evaluates the risks and impact of a wind down and considers how to mitigate them.
- 3.1.2 The objective of wind-down planning is to help to reduce the risk of negative effects for *consumers* and markets when a *firm* winds down its business.
- 3.1.3 The following list is not exhaustive but an effective wind-down plan typically includes the following components:
 - (1) The scenarios that could lead to a *firm* no longer being viable, adequate governance processes, management information monitoring and other control processes to support timely wind-down decision making.
 - (2) A plan to steer the *firm* to wind down its business in an orderly manner after a decision to exit the business has been made.
 - (3) An assessment of the resources, both financial and non-financial, that are needed to support an orderly wind down.
 - (4) Proactively identifying and mitigating any material risks or obstacles to orderly wind down, (e.g. issues that could lead to significant *consumer* detriment, or create a significant adverse impact to the financial market(s) or other third parties).
- 3.1.4 The end product of this process is a documented wind-down plan that is approved by the *firm's governing body*, with a nominated *person* ensuring it is continuously reviewed as to its adequacy and remains current and relevant to the *firm's* operations.
- 3.1.5 A wind-down plan is meant to be a living document, refreshed periodically and after any material change in business/operating model (e.g. addition of new major business line). It is good practice for the *governing body* to approve every revision.
- 3.1.6 We know that some *firms* may have carried out similar planning exercises under other regulatory processes (e.g. *ICAAP*, *RRD*). This approach document does not replace or re-

interpret those processes. However, *firms* may want to take this approach document into account to further strengthen their wind-down planning.

[**Note:** Internal Capital Adequacy Assessment Process (*ICAAP*) is for *firms* which are subject to *CRD IV / BIPRU*. Some of these *firms* are further subject to the Recovery and Resolution Directive (*RRD*).]

3.1.7 Some commonly asked questions about wind-down planning:

Q1: If a *firm* is running normally and is generating revenue/profits, would wind-down planning be of any relevance?

Yes. There is no guarantee that a normally functioning *firm* will not fail in the future. *Failure* of a *firm* could occur suddenly. Without proper advance planning, a *firm* running into difficulties has an increased likelihood of a disorderly wind down, leading to *consumer* detriment and/or potentially adverse effects in the market.

Q2: What is the difference between business continuity planning (BCP) and wind-down planning?

Most *firms* would have been requested to submit a description of business continuity and disaster recovery plans when they were authorised. BCP focuses on the *firm's* ability to continue to function or recover despite unforeseen physical and/or technical interruptions to its business. The *firm's* assumption is that it will remain a going concern and so the BCP's focus is on resilience.

On the other hand, wind-down planning deals with situations in which the business is no longer viable or the *firm* makes a strategic/business choice to exit their regulated business. The *firm's* assumption is that, for example, it will not remain a going concern or deliver the desired return on capital and so the focus is on how it can wind down its activities and relinquish its regulatory *permissions* in an orderly manner.

Q3: Which scenario is the most appropriate for the purpose of wind-down planning?

There are various scenarios which may lead to the wind down of a *firm* (i.e. wind-down scenarios), such as loss of key *client(s)* or a severe economic downturn.

There is no single wind-down scenario that applies to all *firms*. The most useful scenarios to support forward planning are those that are severe, relevant to the *firm* and may result in the business not being viable.

Wind-down planning allows *firms* to plan ahead so that they have adequate financial and non-financial resources to:

- (a) formulate judgement if they have become unviable;
- (b) explore recovery options and/or mitigating actions (e.g. potential capital injections); and
- (c) wind down the business in an orderly manner if no other option is available.

3.2 Time horizon and the people involved in the planning process

- 3.2.1 This section explains the time horizon (including the likely starting point and end point of the wind-down period), and some of the associated activities and costs firms may want to take into account during the wind-down planning process.
- 3.2.2 The starting point of the wind-down period is when the firm’s governing body (e.g. the Board of Directors of a company) makes the decision to wind down its regulated business. Note that after making the decision to wind down, the *firm* is no longer a going concern.
- 3.2.3 The end point of the wind-down period is when the *FCA* cancels the *firm’s Part 4A permission*.
- 3.2.4 However, wind-down planning is not just about the events during the wind-down period (i.e. between the start point and end point as described above). It also includes what precedes the actual wind-down process. In particular, as wind down can be triggered by a range of scenarios, firms that proactively identify and monitor key management information, relevant metrics and early warning indicators are likely to be better prepared. It can also support more effective decision making and, where appropriate, timely initiation of the wind-down plan if needed.

Illustration of the time horizon

Considerations during Business as Usual	Wind-down period		
	Start point	During wind-down period	End point
<ul style="list-style-type: none"> - Consider a range of wind-down scenarios - Identify relevant management information to be monitored - Governance process and <i>internal controls</i> are in place 	A <i>firm’s governing body</i> makes a decision to wind down	A <i>firm</i> wants to close down its business in an orderly fashion and needs sufficient financial and non-financial resources to do so.	Cancellation of <i>permission</i>
In the event of business difficulties, a <i>firm</i> may try to recover and/or pursue other mitigating actions (e.g. find a potential investor).	After making the decision to wind down, the <i>firm</i> is no longer a going concern.		

- 3.2.5 Given the significance of wind-down planning, the governing body of a firm is most likely to be accountable for it, with appropriate engagement of relevant experts across the firm and, if required, externally. Senior individuals typically lead the wind-down process, and are accountable to the governing body. The following table illustrates how different individuals or business areas could be involved in wind-down planning.

Illustration of who could be involved in wind-down planning

<i>Governing body</i> (e.g. Board of Directors)	The <i>firm's governing body</i> considers and approves the wind-down plan. This may include challenge from <i>non-executive directors</i> if relevant.
<i>Senior management</i>	The planning process is likely to be most effective if it is led by an appropriate accountable <i>person(s)</i> reporting to the <i>governing body</i> . For a very large <i>firm</i> or <i>group</i> of firms, a further working group may be created to help coordinate and deliver the process. <i>Senior management</i> , e.g. CEO, CFO, CRO, COO, provide valuable input to the review, validation and challenge, before the plan is presented to the <i>governing body</i> for deliberation.
Front line business and support areas	Front line business and support areas are engaged to understand and mitigate potential operational issues and challenges from the wind-down process, e.g. redundancies, IT systems, access to third-party services, etc.
Relevant external experts/third parties	<i>Firms</i> may find it useful to consult external experts (e.g. an insolvency practitioner) and other relevant third parties to improve their understanding and management of key wind-down issues/scenarios.

[**Note:** The above table is an illustration, rather than a definitive list. *Firms* may need to analyse their organisational structure, business model and operating model to decide on the appropriate participants.]

3.3 Wind-down scenarios: What would make a firm no longer viable?

3.3.1 There are many reasons why a *firm* may wind down, including a strategic exit where the *firm* makes a business decision to exit and the decision is not due to it being unviable.

3.3.2 However, our approach document focuses on dealing with scenarios in which a *firm* is no longer viable. We refer to these as wind-down scenarios and these are typically used to inform a *firm's* wind-down plan. A *firm* will probably identify more than one wind-down scenario.

3.3.3 To do this, *firms* may want to consider what events would be likely to make it no longer viable. A *firm* is not viable if it no longer has adequate financial or non-financial resources to carry on its *regulated activities*. This could happen for a variety of reasons, including:

- (1) significant financial *losses* with no signs of timely recovery;
- (2) loss of key *clients* without realistic prospect of their replacement in good time; and
- (3) loss of critical infrastructure (e.g. essential IT systems) with no signs of timely recovery.

3.3.4 A *firm* may consider the following factors when formulating its wind-down scenarios:

- (1) business and operating models (business models show how a *firm* makes money, obtains funding and maintains healthy *cash* flow while operating models look at the day-to-day operations of the business);
- (2) key revenue drivers, *clients* and functions in its operating model; and

- (3) vulnerable areas in its business and operating models.

There may be other factors a *firm* may want to consider.

3.4 Effective risk management

3.4.1 A good wind-down plan is most likely to be supported by an effective risk management framework. This may include:

- (1) a clear risk appetite that has been approved and validated by the *governing body*;
- (2) analysis of wind-down scenarios;
- (3) appropriate reporting and monitoring of management information, risk metrics and early warning indicators; and
- (4) any potential recovery options.

3.4.2 A clear risk appetite, as well as an effective risk identification and assessment approach, are important parts of wind-down planning. They can help to identify the risk metrics that need to be monitored and to set the appropriate thresholds.

3.4.3 Well-structured management information can help to identify emerging risks that could lead to a wind-down scenario. For instance:

- (1) funding institutions are reconsidering terms/conditions of credit facilities provided to the *firm*;
- (2) approaching the date of contract renewal with a key client; and
- (3) profit and loss account pressure due to poor market conditions.

3.4.4 Good reporting processes can help ensure that the *firm* can assess emerging situations as soon as possible and intervene appropriately (i.e. attempt to recover).

3.4.5 A *firm* may consider setting thresholds for relevant management information (e.g. profitability, capital adequacy, liquidity), so that if the data shows breaches of the threshold values it can trigger a report to *senior management* and prompt thinking on the next steps.

3.4.6 *Firms* may consider potential options for recovery in the face of adverse business conditions, such as selling part of its business or seeking capital injection). This is known as recovery planning. Even if a *firm* has carried out recovery planning, wind-down planning can still be relevant as there is no guarantee that recovery options would save the *firm's* business.

[**Note:** Some firms are required to prepare recovery plans, i.e. those subject to the Recovery and Resolution Directive (*RRD*).]

3.5 Making a decision to wind down

3.5.1 In the event of a severe stress, a *firm* may have one or more potential options that might enable it to recover and return to a normal or sustainable position, for example, finding potential investors to acquire or invest in the failing business. However, in spite of management actions, there may be no effective way to recover from a severe stress.

- 3.5.2 The *firm's governing body* will need to make the decision to wind down in a timely manner. The wind-down plan can help the *firm's governing body* evaluate how viable any potential recovery options are against the risk of a disorderly *failure* if the decision to wind down is delayed or deferred for too long.
- 3.5.3 Establishing clear indicators and thresholds can help a *firm's governing body* to make timely decisions. They can also refer to the *firm's* wind-down scenario analysis to provide an indication of the minimum financial and non-financial resources needed to ensure the orderly winding down of the *firm's* activities. Deferring the wind-down decision to a point where that level of resources is no longer available would significantly increase both the risk and scale of a disorderly *failure*.
- 3.5.4 *Firms* may identify what *regulated activities* they will cease once the wind-down decision is made. For instance, a *firm* should not take on any more new *clients* once that decision is made.
- 3.5.5 We remind *firm's senior management* that they need to be aware of their *directors'* duties and what they must not do if the *firm* becomes insolvent.
- 3.5.6 If the *governing body* takes the decision to wind down, a *person* or group will probably need to be given the role of coordinating, directing and implementing the wind-down process. Many elements of these governance, oversight and operational arrangements can be established in principle in advance as part of a *firm's* wind-down planning.
- 3.5.7 *Firms* should inform the *FCA* as soon as there are signs of a potential *failure* or any other causes for winding down. They may also want to start communications with various stakeholders. See Section 4.2: Communications plan.

[**Note:** See Principle 11 (Relations with regulators) (*PRIN 2.1.1R*) for more information about notifying the *FCA* as soon as there are signs of potential *failure* or causes for winding down.]

3.6 Impact assessment: Who will be affected by the wind down?

- 3.6.1 It is important, given the *FCA's* *consumer* protection and market integrity objectives, that *firms* seek to identify and mitigate any adverse impacts on *consumers*, *counterparties* and the wider markets that might arise as a result of a wind-down decision. A thorough analysis of all stakeholders will help a *firm* identify who would be affected if it winds down. It also helps a *firm* to understand how difficult it will be to wind down, for example, if it has many non-cancellable contracts in place which will inevitably increase the costs of winding down and prolong the length of the wind-down period.
- 3.6.2 We expect *firms* to treat *customers* fairly during the wind-down period. This is particularly important if a *firm* is holding *client monies* and *custody assets* (see Section 4.3: Client monies and custody assets) or is offering services to potentially vulnerable *customers*.

- 3.6.3 *Firms* are required to keep up-to-date *client* records. These will prove invaluable in assessing the number and types of *consumers* who may be affected by the wind down.
- 3.6.4 *Firms* can support their Impact Assessment by a risk assessment of each stakeholder group along with the mitigating actions the *firm* would consider appropriate. Some factors that a *firm* may consider include:
- (1) How quickly can a firm conclude any outstanding transactions? Will there be any tax or other implications to customers?
 - (2) Can the *firm* help transfer its *customers* to another *financial institution*? If the *firm* has many *customers* to be transferred out, do other *firms* in the same sector have the capacity to take them on?
 - (3) How quickly can *client monies* and *custody assets* be returned?

Market participants

- 3.6.5 An orderly wind down minimises the impact on the wider market. Some participants in the market may be more affected than others, for example if the *firm* is a major product provider for a particular sector, in which case its winding down may cause a greater impact than would otherwise be the case.

Employees

- 3.6.6 A *firm* may need to consider relevant employment legislation, especially if it has businesses that involve *overseas* jurisdictions. It may also choose to identify who needs to be retained during the wind-down period to help with the wind-down operation, for example, compliance and contact centre *employees*.
- 3.6.7 Although it may seem less critical to include consideration of other third parties such as landlords, creditors or trade payables, *firms* will need a prudent approach to wind-down planning factors and the effect of winding down on third parties that have contractual relationships with the *firm*, such as the landlord of the *firm's* office. This ensures that essential needs, such as premises, are still provided for during the wind-down period. It may also avoid a defaulting creditor triggering insolvency proceedings against the *firm* in anticipation of its exit.

3.7 Operational analysis: What happens during the wind-down period?

- 3.7.1 The wind-down period can be considered as a timeline along which steps are taken, from making the wind-down decision all the way to the *FCA* cancelling the *firm's permission*.
- 3.7.2 These steps are effectively a function of, and in turn affect, a *firm's* entire business. A *firm* may find it useful to assess the following non-exhaustive list:
- (1) The industry and the sector it operates in and the impact it may cause to the markets when it winds down.
 - (2) Who the *firm's clients* are and what processes are in place to maintain *client* records.
 - (3) Dealing with *client complaints*, particularly post winding down.
 - (4) Legal and regulatory status (including *FCA permission*).

- (5) Applicable legal, regulatory and insolvency regimes. This will include, for instance, *directors'* duties under company law.
- (6) Organisational structure and operating model.
- (7) Internal processes, systems and human resources.
- (8) Processes or systems that are interconnected and/or outsourced.
- (9) Existing contractual commitments, such as with *employees* or third parties.

In particular, there may be restrictions or penalty clauses for breaking contractual relationships.

3.7.3 After conducting its assessment a *firm* can work out an outline of sequenced actions in a wind-down scenario and how long each action will take. The specifics vary from *firm* to *firm* but some possible considerations include:

- (1) How would the *firm* announce the wind-down decision and manage communication with stakeholders?
- (2) How would the *firm* deal with redundancies of *employees*?
- (3) Who needs to be available to assist the winding down?
- (4) What systems (e.g. IT systems) need to be available for the wind down?
- (5) How will the *firm* reconcile *clients'* business records and ensure their interests are not affected? For instance, a *firm* will have to return *client monies* and client assets during wind down.
- (6) When might the *firm* need to engage professional advisors, such as an insolvency practitioner to support the wind-down process?

3.7.4 The *firm's governing body* will need to take ultimate ownership of, and accountability for, the timely implementation of the wind-down plan. However, for each step or activity this analysis identifies, it may be helpful to indicate who will be responsible for that particular task.

3.7.5 At the end of the analysis, the *firm* would be better able to estimate the length of the wind-down period.

3.8 Resource assessment

3.8.1 To achieve the objective of winding down in an orderly manner, a *firm* needs to have adequate financial and non-financial resources to do this and would ask itself a range of questions:

Non-financial

3.8.2 What non-financial resources, such as premises, IT, key *employees*, external advisors etc, does it need to carry out the steps identified in the operational analysis and for how long does it need them (See Section 3.7: Operational analysis: What happens during the wind-down process?)?

3.8.3 If a *firm* relies on outsourced services, will these services still be available during the wind-down period?

3.8.4 If a *firm* is part of a larger *group*, and is depending on *group* resources, would it still have adequate resources to wind down in an orderly manner if the *group* failed?

Financial

3.8.5 This approach document does not provide any *rule* or interpretation in addition to the financial resources requirements applicable to a *firm*. Rather, it highlights some of the factors which a *firm* may want to consider in its wind-down planning.

3.8.6 It is important that *firms* monitor their solvency on a regular basis to ensure they continue to be able to meet their obligations as they fall due. If a *firm* becomes uncertain of its ability to do so, it may seek professional advice, such as from an auditor or insolvency practitioner to assist.

3.8.7 A *firm* in wind down will have non-routine *cash* inflows and outflows, which are best monitored on a daily basis. This includes:

- (1) inflows, i.e. predicted revenue and other inflows that are likely to be limited after the triggering event and/or if a wind-down decision is made;
- (2) ordinary outflows, i.e. the cost of maintaining operational premises and systems; and
- (3) extra-ordinary outflows associated with winding down, such as extra closure costs, legal fees, professional services and insolvency practitioner *fees*, redundancy payments, retention payments, pension fund deficits, lease and other termination penalties and costs of breaking contracts.

3.8.8 A *firm* could then consider if it would have enough *cash* or *cash* equivalent investments to meet their operating expenses and any other obligations during the wind-down period.

3.9 Cancellation of permission

3.9.1 A *firm* needs to have its *Part 4A permission* cancelled in order to complete the wind-down process. Before we can grant a cancellation, we will review, amongst other things:

- (1) generally, whether it would be detrimental to *customers* or would cause market disruptions to cancel the permission;
- (2) whether there any unresolved *customer complaints*;
- (3) whether all *client monies* and client assets (if any) been returned in accordance to *CASS rules*; and
- (4) whether there are any outstanding *fees* owed to the *FCA*?

[Note: Although we aim to complete a cancellation transaction as quickly as possible, we will need sufficient time to consider if a *firm* meets the regulatory requirements or prerequisites for cancellation of permission.]

4 Further topics

4.1 Anticipating reactions

4.1.1 In Section 3.6: Impact assessment: Who will be affected by the wind down?, we explained how important it is for *firms* to assess the impact of a wind down on *customers*, markets and other parties. In this section, we highlight the importance of anticipating the reactions of those parties.

Employees

4.1.2 *Employees* may want to leave as soon as possible to secure new jobs. *Firms* may therefore need to consider how to ensure it can retain the key *employees* needed to carry out the wind down.

Clients or counterparties

4.1.3 If a firm is winding-down, especially under challenging market conditions, there is a risk that *counterparties* or *clients* may simply *default*. This may have consequences on the anticipated cost, duration and or impact of the wind down.

Creditors, landlord and other suppliers

4.1.4 When a *firm* announces its wind-down decision, this may affect its reputation and credit rating. This may cause concerns for creditors, landlord and other suppliers about the *firm's* ability to meet any outstanding liabilities and trigger reactions such as margin calls or demands for full and final payment. It is therefore crucial that the *firm* communicates with these parties, and ensures there is sufficient liquidity to meet the liabilities when they fall due. This is a prime example of the importance of making a timely decision to wind down.

4.2 Communications plan

4.2.1 An effective wind-down plan would include a predetermined communications plan that considers the contents and timing of communications, including website updates, to a wide range of stakeholders, such as relevant regulators (e.g. listing authority, stock exchange, *FCA/PRA*, *overseas* regulators etc.), *employees*, *customers*, service providers, *shareholders*, bondholders and media.

Some suggested elements for the communications plan:

- 1) identify the stakeholders to be engaged;
- 2) who and how to engage those stakeholders;
- 3) agree the internal process for drafting and approving any communication to the stakeholders;
- 4) establish guidance and procedures for a proactive vs reactive communication strategy (or combination);
- 5) prepare scripts in advance if appropriate e.g. holding statements, acknowledging that detailed messaging may only be possible reactively; and
- 6) recognise the potential need for the *governing body* to engage with legal advisors and communication experts (e.g. media training).

- 4.2.2 Good stakeholder contact during the wind-down period supports the *FCA's consumer protection and market integrity statutory objectives*. Rumours and a lack of reliable information can create concerns amongst *consumers* and, in more severe cases, increased risk of detriment and disruption to the wider market.
- 4.2.3 In line with Principle 11, *firms* need to be mindful of their obligation to keep the regulator informed of material developments. This includes issues that might threaten the ongoing viability of the *firm* and any decision to cease operations. Thereafter, a regular dialogue between the *firm* and the regulator needs to be maintained.
- 4.2.4 It is important to identify one or more individuals who will be responsible for coordinating effective and timely communications during the wind-down period. These individuals are likely to include senior decision makers as well as those with specialist communications/technology skills, for example those with knowledge of financial disclosure requirements, web publishers etc. This is particularly relevant for a *group* of companies, or where *listed* entities are involved. In order for these individuals to effectively deliver communications in a wind down they will need the appropriate training, tools, systems and resources.

4.3 Client monies and custody assets

- 4.3.1 Any *firm* holding *client monies* or *custody assets* must ensure that it complies with all applicable *CASS rules*.
- 4.3.2 All firms that fall under the requirements of *CASS 10.1.1R* must maintain a *CASS Resolution Pack (CASS RP)*.
- 4.3.3 The purpose of the *CASS RP* is to ensure that a *firm* maintains and is able to retrieve information that would, in the event of its insolvency, help an insolvency practitioner achieve a timely return of *client money* and *safe custody assets* held by the *firm* to its *clients*.

4.4 Groups of firms and overseas businesses

- 4.4.1 If the *firm* is part of a larger *group* and decides to have an individual wind-down plan the latter will almost inevitably be impacted. In particular, some or all elements of its governance, financing and operations may be dependent on the *group*. These dependencies have implications on the wind-down plan's cost, duration and simplicity.
- 4.4.2 A *firm* preparing a wind-down plan at *group* level would be facing two possible wind-down scenario options:
- (1) the *firm* winds down on its own in an event independent of its *group*; or
 - (2) the *firm* winds down as part of a larger *group failure/wind-down* event.

4.4.3 The following are just some common questions which a *firm* could consider in a *group* scenario:

- (1) Does the *group*/parent need to be consulted before making the wind-down decision?
- (2) If the *group* has entities that are *listed*, are there any actions to be taken in line with applicable *listing rules* and disclosure regimes?
- (3) If there are *intra-group transactions*, how are they unwound and how do they affect wind-down costs?
- (4) What support will the *firm* receive from the *group* during its wind-down?

4.4.4 A *group failure* event is particularly serious, as it could mean the relevant *firm* no longer has access to *group* resources such as a central treasury function, financial resources, IT and administrative functions for its own wind-down operation. It would then need to consider alternative resources in its wind-down planning.

4.4.5 Wind down triggers the closure of all regulated business undertaken by the *firm*, including *overseas* activities. Closure of *overseas* branches or subsidiaries could be complicated due to jurisdictional differences (e.g. regulatory requirements, employment law, law on liquidation, etc.) and time differences (e.g. in relation to announcement of wind down, closing off transactions etc.), which can add to the cost and duration of winding down.

Appendix 1: Quick Reference Guide (QRG)

1. Introduction

1.1 Overview

- 1.1.1 This Quick Reference Guide (QRG) helps solo-regulated *firms* to put the theory of wind-down planning into practice.
- 1.1.2 This QRG is **not** a definitive checklist for wind-down planning. No two *firms* are identical and the actual wind-down planning process will depend on a *firm's* specific business and operating model. This QRG highlights the various components a *firm* can include when building its wind-down plan.
- 1.1.3 This QRG is written for all solo-regulated *firms*, but it may be particularly helpful to those carrying out wind-down planning for the first time.

1.2 Main concepts

- 1.2.1 A *firm* will have to wind down if continuing its business is no longer viable. A business is no longer viable if the *firm* does not have adequate resources to meet its regulatory requirements (e.g. the threshold conditions) or to wind down in an orderly manner.
- 1.2.2 Well-structured management information allows a *firm* to identify if there are any emerging risks that may make the *firm* unviable. This may allow a *firm* some time to try to recover. If the recovery options fail, then it is almost certain that it is no longer viable.
- 1.2.3 A *firm* needs to be careful not to leave the decision to wind down so late that it no longer has adequate resources or liquidity in order to wind down in an orderly manner.

2. Leadership and responsibilities

2.1 Leadership and responsibilities

- 2.1.1 For successful wind-down planning, it is important that a *firm's governing body* (e.g. the board of *Directors* of a company or *partners* of a *partnership*) fully understand the purpose and process of wind-down planning.
- 2.1.2 The *firm's governing body* is ultimately responsible for the effectiveness of wind-down planning, and so needs to demonstrate leadership and set the strategy for the process.
- 2.1.3 Effective wind-down planning is more likely if it is prepared by a working group leading the process and reporting to the *governing body*.

Effective	Less effective
Board of <i>Directors</i> appointed the Chief Operating Officer (COO) to lead the wind-down planning project and asked the COO to brief the Board on the principles of wind-down planning so it can agree on the planning strategy.	Board of <i>Directors</i> asked the Finance Department to work out the estimated costs of winding down the business (i.e. without considering the associated governance and operational planning elements).

3. Business areas and workshops

3.1 Engaging all business areas and setting up workshops

- 3.1.1 All the *firm's* business areas, including the front line, are affected by winding down and will bring their unique perspectives to crafting a strategy and a working document.
- 3.1.2 A sensible approach is to set up workshops with representatives from various business areas. The workshop will explain the principles of wind-down planning to these representatives and work with them to analyse the processes and resources of each business area.
- 3.1.3 These workshops will provide the data to be used in the wind-down planning.

<p><u>Effective</u> <i>Firm</i> sets up a workshop for each business area. Explains the rationale of wind-down planning to the representatives in the workshop, and invites the representatives to explain their local business area processes, risks and resources.</p>	<p><u>Less effective</u> <i>Firm</i> sends a questionnaire to each business area and asks someone in that area to fill in the form and return it to <i>senior management</i>.</p>
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4. The business and operating models

4.1 Analysing the business and operating models

- 4.1.1 In order to analyse the business and operating models effectively, a *firm* should:
 - (1) place emphasis on understanding how the *firm's* balance sheet generates profit and loss figures and the details of operations;
 - (2) carry out a review the sources and uses of both capital and liquidity by reviewing, among other items, revenue drivers, cost drivers and sources of *cash* inflows and outflows;
 - (3) consider which areas may be difficult to wind down, e.g. due to longer notice periods of some *employees*, certain *transactions* or contracts with third parties that are subject to a longer cancellation period; and
 - (4) consider internal and external connectedness.

<p><u>Effective</u> The working group carefully studies the data gathered from the workshops, and assesses which areas may be difficult to wind down.</p>	<p><u>Less effective</u> The working group does not draw out from the data gathered from the workshops vulnerabilities and pinch points.</p>
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5. Wind-down scenarios and relevant management information

5.1 Generating wind-down scenarios and identifying relevant management information to monitor

5.1.1 In order to generate wind-down scenarios, a *firm* may consider the followings:

- (1) which are the critical revenue drivers and business lines for the *firm* to sustain;
- (2) which are the business areas subject to the greatest risks, e.g. if a sudden large volatility in the currency market will lead to great *losses*;
- (3) the infrastructure, resources or third parties upon which the *firm* heavily depends;
- (4) the *firm's* agreed (qualitative and quantitative) risk appetite and risk thresholds;
- (5) internal audit reports;
- (6) compliance monitoring processes and reporting.

5.1.2 The above thinking will help a *firm* to find out its 'risk fault lines', i.e. those critical areas whose *failure* would severely affect the business.

5.1.3 Based on the risk fault lines identified, a *firm* can decide the plausible scenario(s) – the wind-down scenarios - under which it will no longer be viable. We give some examples in the table at 5.1.4.

5.1.4 After defining the wind-down scenario(s), a *firm* identifies the key management information that is most directly related to those scenario(s) and the relevant indicators it will want to monitor for danger signs.

<p><u>Effective</u> Some wind-down scenarios (fast and slow-moving; <i>firm</i> specific and macro-economic):</p> <ul style="list-style-type: none"> • severe economic downturn leading to continuous <i>losses</i> with no sign of recovery; and • loss of critical IT infrastructure (especially if the <i>firm's</i> business is largely technology-based). <p>Some management information which a <i>firm</i> could constantly monitor:</p> <ul style="list-style-type: none"> • profitability; and • net <i>cash</i> position. <p>[Note: these are not definitive lists. <i>Firms</i> will need to analyse their business and work out their own scenarios.]</p>	<p><u>Less effective</u> The <i>firm</i> takes the view that the <i>firm</i> is running well and will never fail. Even if it failed, it believes that it could sell the business to another <i>firm</i> in short order or obtain generous <i>cash</i> infusions from a parent.</p> <p>[Note: No business can categorically guarantee it will never fail. A failing business is not always able to find an acquirer/investor for the business and the process to effect due diligence and a change in control can be very lengthy.]</p>
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6. The governance process for winding down

6.1 Formulating a governance process for winding down

- 6.1.1 The Board ultimately owns any documented governance process for winding down. It may stipulate a mechanism to determine when to invoke wind down, typically via monitoring key management information to detect the early warning signs of a potential wind-down situation. The Board may also state a line of reporting to ensure that *senior management* and the *governing body* is given this information without delay.
- 6.1.2 In a time of financial stress, clear-headed and prompt decision-making is essential. It is up to the *governing body* of a *firm* to make such a decision, but it may have to consult its parent if it is part of a larger *group*.

7. Impact assessment

7.1 Carrying out an impact assessment: who will be affected?

- 7.1.1 In an impact assessment, a *firm* may ask the following questions to identify the stakeholders who may be affected by the winding down:
 - (1) Consider how the *customers* would be affected by the wind down. For instance, how many existing *customers* will the *firm* have to deal with if it is winding down now? How will the *firm* close *transactions* with these remaining *customers* and will *customers* be diligent in responding to the *firm's* notices and closing their business relationship?
 - (2) Does the *firm* need to execute risk-reducing trades and, if so, will it continue to have access to the right market *counterparties* to do so?
 - (3) Does the *firm* have an effective system to maintain *client* and *transactions* records?
 - (4) How will *employees*, suppliers, *counterparties* or other third parties be affected?
 - (5) What are the potential tax implications of winding down?

<p><u>Effective</u> Take into account the possibility of <i>customers</i> disputing <i>transactions</i> when closing out.</p>	<p><u>Less effective</u> Take the attitude that if a <i>firm</i> is insolvent, the administrator will ultimately allocate the assets according to priority.</p>
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8. Operational analysis

8.1 Operational analysis

- 8.1.1 In an operational analysis, a *firm* may adopt the following structure to work out what steps may need to be taken in winding down:
 - (1) The start point of the wind-down timeline is when the wind-down decision is made. The end point is when the regulatory *permission* is successfully cancelled.

- (2) Numerous actions need to occur after the wind-down decision is made and these populate the timeline in sequence.
- (3) The estimated length of the wind-down period can then be calculated from the sequence of the individual actions' durations.
- (4) This in turn allows an assessment of what resources (financial and non-financial) would be needed to implement it.

Factors which a *firm* may consider:

- How would the *firm* announce the wind-down decision and manage communications policy?
- Who needs to be available to assist the winding down?
- How would the *firm* deal with redundancies and, conversely, which *employees* need to be retained with special financial arrangements?
- What systems (e.g. IT systems) need to be available during the winding down?
- How will the *firm* reconcile *clients'* business records and ensure their interests are not affected? For instance, if a *firm* has to return *client monies* and *assets* when winding down, how would it do this?
- Will the *firm* need to engage professional advisors to wind down?
- Has the *firm* considered the implications for any *overseas* offices and branches?

9. Time and costs for wind down

9.1 Estimating the time necessary and costs for wind down

9.1.1 *Firms* may take into account the followings in order to estimate the time and costs needed for wind down:

- (1) *Firms* should not take on new *clients* after a wind-down decision is made, but there may be a continuing income stream from contracts with existing *clients* before the cancellation period is over. *Firms* may however want to consider how certain these remaining income streams will be in the context of winding down.
- (2) *Firms* then need to estimate the costs of winding down. These costs include redundancy payments, retainer premiums for essential *employees*, legal and other professional *fees*, or cancellation penalties with third party providers.
- (3) *Firms* need to determine, conservatively, the time necessary to the point that the *FCA* would remove the *firm's* Part 4A permission.
- (4) *Firms* may draw out these estimated revenue and costs on a month-by-month schedule covering the entire wind-down period.
- (5) The estimated wind-down costs may also take into account the possible need for an administrator and all other wind-down conditional costs such as tax, legal, specialist consultancy and audit.

Effective

The *firm* sets out a month-by-month schedule of revenue and costs in the wind-down period. Costs are itemised and conservatively estimated.

Less effective

The *firm* estimates costs on a quarterly basis. **[Note:** Though this is not necessarily wrong, this would make it difficult to assess if the *firm* would have enough *cash* or liquid assets to meet its expenses on a monthly basis.]

10. Adequacy of financial and non-financial resources to wind down

10.1 Assessing the adequacy of resources

10.1.1 A *firm* may take into account the followings to assess if it would have adequate resources to carry out a wind down:

- (1) To achieve an orderly wind down, a *firm* needs to have adequate financial and non-financial resources. A *firm* that leaves making the decision to wind down until it is too late risks breaching regulatory requirements, engaging in a disorderly wind down, or even operating illegally while insolvent.
- (2) Assess whether the *firm* has sufficient *cash* to meet monthly expenses during the wind-down period.
- (3) Determine what non-financial resources are needed to achieve orderly wind down and check they have been secured.

<p><u>Effective</u> Consider which key <i>employees</i> will be needed for an orderly wind down but may want to leave the <i>firm</i> after the wind-down decision is made. An allowance to retain <i>these employees</i> during the wind-down period may be needed.</p>	<p><u>Less effective</u> The <i>firm</i> only assesses its capital adequacy, and fails to assess its ability to meet monthly expenses during the wind-down period.</p>
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11. Special considerations

11.1 Special considerations

11.1.1 Please refer to Chapter 4 of the approach document and identify which factors apply and consider incorporating them into the wind-down planning

11.1.2 In particular, if a *firm* has any dealing with *client monies* and *assets*, it needs to ensure it complies with the relevant *rules* in CASS.

11.1.3 *Firms* should also consider to have communications plan in place.

12. Documentation, approval and maintenance

12.1 Documentation, approval and maintenance

12.1.1 *Firms* may keep a written record of discussion of the wind-down planning process, and most importantly, the wind-down plan as the final output.

12.1.2 The final output - the wind-down plan - will be easier for its future users to implement if it is simply structured for ease of reference with sections such as:

- (1) governance process for wind-down scenario (Section 6 of the QRG);
- (2) operational analysis for winding down (Section 8 of the QRG);

- (3) estimated revenue/costs schedule of wind down (Section 9 of the QRG); and
- (4) resource assessment (Section 10 of the QRG).

12.1.3 The *governing body* of a *firm* should review and approve a wind-down plan and then maintain it by designating an accountable individual to own the document. This maintenance will ensure its reliability as an effective resource for the *firm*.

<u>Effective</u> Wind-down plan is kept as a live document and is reviewed at least once a year.	<u>Less effective</u> Wind-down plan is left unrevised for years.
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