

Memorandum of Understanding between the Prudential Regulation Authority and the Financial Services Compensation Scheme Ltd.

Purpose and Scope

1 The Financial Services Compensation Scheme (the Scheme) exists, under the Financial Services & Markets Act 2000, as amended, (FSMA) to provide protection for eligible customers of failed financial services firms. The Scheme protects customers that incur financial losses when firms authorised under FSMA are unable, or likely to be unable, to satisfy claims against them relating to deposits, life and general insurance policies, investment business, advice and arranging of mortgage business, and insurance broking. The Scheme is administered by Financial Services Compensation Scheme Ltd (FSCS).

2 The firms concerned are authorised by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) or, in some cases, authorised by the FCA only. As set out below, the FCA and the PRA can each set some of the rules relating to the Scheme and to its operator, the FSCS.

3 This Memorandum of Understanding (MoU) sets out the framework agreed between the FSCS and the PRA. It has been agreed in fulfilment of section 217A(2) of FSMA which places the FSCS and the PRA under a duty to co-operate and to maintain a memorandum describing compliance with that duty.

Roles and responsibilities of the PRA

4 The PRA is responsible for the authorisation, in conjunction with the FCA, and prudential supervision of individual deposit takers (including banks, building societies and credit unions), insurers (including friendly societies) and certain designated investment firms. Its objective is to promote the safety and soundness of dual-regulated firms, and it is required to advance this objective primarily by seeking to minimise any adverse effects of firm failure on the UK financial system and to ensure that firms carry on their business in a way that avoids adverse effects on the system. In the case of insurers, the PRA has the additional objective of contributing, through its prudential supervision of insurers, to securing an appropriate degree of protection for policyholders.

5 As set out in secondary legislation, FSMA (FSCS) Order 2013, the PRA is responsible for writing those rules that determine the arrangements for providing protection in relation to deposits and

insurance provision. The FCA is responsible for writing those rules for all other types of financial activity covered by the Scheme.

6 The FCA and PRA are jointly responsible, under FSMA, for ensuring that the FSCS is capable of discharging its functions.

7 The directors of the board of the FSCS are appointed by the FCA and the PRA. Under FSMA, the FCA and the PRA will jointly seek the approval of HM Treasury in the case of the chairman's appointment. The directors are appointed on terms that secure their independence from the FCA and the PRA. The FCA and the PRA will engage the FSCS on appointments to its board.

Roles and responsibilities of the FSCS

8 The FSCS is established, as required by FSMA, as a limited company. As scheme manager, the FSCS is responsible for administering the Scheme, as it applies to deposits and insurance provision, in accordance with the rules made by the PRA. It administers compensation arrangements for FCA-regulated activities under rules made by the FCA.

9 The FSCS, as scheme manager, is independent from, but accountable to, both the FCA and the PRA for the effective operation of the Scheme. The day-to-day operation of the Scheme is the responsibility of the FSCS and its board.

10 The FSCS is accountable to the PRA for the operation of the Scheme in relation to deposits and insurance provision. A very important element of this includes seeking to establish and maintain a high degree of awareness amongst depositors and policy holders of the protection offered by the Scheme (and when coverage is provided by another EEA scheme). It also involves, with respect to the PRA:

- establishing and implementing procedures to enable the FSCS to deliver its responsibilities to administer the Scheme;
- determining and collecting levies to cover management expenses and the costs of guaranteed payments or transfer to another provider;
- using its resources in an efficient and economic way; and
- reporting to the PRA, as described in this MoU, on how it has delivered its responsibilities.

Information sharing: general

11 The FSCS and the PRA undertake to share information to allow them to fulfil their respective responsibilities.

12 The FSCS will keep the PRA informed in relation to issues concerning the interpretation of rules, the eligibility of claims, and the FSCS's assessment of each firm's capacity to assist the FSCS to pay out quickly. This may include copies of any legal agreements or other information that could materially affect the funding needs or the ability of the FSCS to deliver its responsibilities.

13 In addition, the FSCS will keep the PRA informed of any actual or likely material litigation on its behalf (or against it), particularly those it pursues under the PRA's rule COMP 7.2.3(2) in order to make recoveries and those that could have a material adverse effect on its funding needs.

14 The PRA agrees to keep the FSCS informed of any regulatory or market developments that may affect the planning or operation of the Scheme:

- in times of market disruption, or as the likelihood of a specific firm failing increases, the FSCS and the PRA acknowledge that information sharing will become more intensive;
- and
- this will be the responsibility of the PRA's directors responsible for supervising, respectively, deposit-takers and insurers.

15 The FSCS will keep the PRA informed on the effectiveness of the rules for the Scheme, including on public and customer awareness of the deposit and insurance arrangements.

Confidentiality

16 The FSCS and the PRA will protect the confidentiality and sensitivity of all unpublished regulatory and other confidential information received from the other party.

17 Where one party has received information from the other, it will consult before passing the information to a third party, unless it is shared with relevant governmental or regulatory organisations, including the Bank of England, HM Treasury, and the FCA.

18 Some relevant information may be received from third parties. Each party's ability to share such information with the other may in some instances be constrained by legal obligations. Both parties will seek to ensure that these instances are minimised.

19 The FSCS and the PRA will liaise, where relevant, on responding to enquiries from the public, including Freedom of Information requests made to the PRA. The FSCS and the PRA will also liaise concerning requests made by individuals for access to data held about them under the Data Protection Act. In all cases, one will consult the other, or seek consent if necessary, before releasing information originally belonging to the other.

Policy making

20 The PRA will seek advice from the FSCS in relation to domestic and international policy making initiatives relating to deposit and insurance compensation arrangements, as appropriate, including where those might have a material effect on the FSCS's ability to administer the Scheme effectively now or in the future.

21 The FSCS will seek advice from the PRA on matters of common interest prior to their discussion at various fora including the International Association of Deposit Insurers and the European Forum of Deposit Insurers (or at any equivalent organisations for insurance if they were to be established in the future).

22 The FSCS and the PRA agree to allow reasonable time, where appropriate, for each other to provide considered comments on material policies, consultations, and rules before they are made public. This does not include announcements in relation to defaults.

Supporting the resolution of regulated firms

23 The FSCS will provide information, where requested, to support the PRA's assessment of a firm's resolvability and the likelihood that any failure would be orderly.

24 The PRA will seek to ensure, through the operation of the Proactive Intervention Framework, that the FSCS has reasonable notice of activity where the PRA may require significant involvement from the FSCS. This involvement may include detailed planning for major defaults including any potential trigger of the Special Resolution Regime (SRR), significant claims to the Scheme, and any other relevant activity.

25 In the event that the SRR, operated by the Bank of England, is triggered for a deposit-taker then the FSCS may:

- under the Bank Insolvency Procedure, make or arrange payments to or in respect of eligible depositors, or make money available to facilitate the transfer of accounts of eligible depositors; or
- be required, where stabilisation powers are used, to arrange for the scheme to contribute to the costs of the resolution.

26 In support of the PRA, the FSCS will assist in monitoring the readiness of bank systems to conduct a rapid payout, including through the verification of deposit-takers' ability to provide a 'single customer view'. Also, the FSCS will keep the PRA informed of its scenario planning and preparedness to deliver on rapid payouts that are within its capability including if it believes there is a material risk that it would not be able to meet the target of seven days for pay out for the majority of depositors. It will ensure that, at all times, the PRA is kept informed of the FSCS's procedures for coping with a significant failure of a firm that is beyond the capability of its existing dedicated staff and resources. .

27 The FSCS will inform the PRA if the type and volume of enquiries it receives indicates high or unusual public concern about particular firms.

Funding, levying and treasury management

28 As set out under FSMA, the FCA and the PRA will determine an agreed split of the FSCS's management expenses for each financial year based on the PRA having responsibility in relation to deposits and insurance provision and the FCA having responsibility for the remainder. The resulting limit is set before the end of the preceding financial year. In order for the FCA and the PRA to be able to consult on the limit, the FSCS will provide to each of them its proposed budget for management expenses and its plan for review and discussion. This will be in accordance with an agreed reporting timetable and format. The FCA, the PRA and the FSCS will co-ordinate the public consultation on the management expenses limit and the FSCS's budget.

29 The FSCS will advise the FCA and the PRA if circumstances change so that it is or may become unable to deliver its responsibilities within the current limit on management expenses. The FSCS will not incur expenditure in excess of its agreed budget unless there is an exceptional and unavoidable

cause (such as an unforeseen rise in claims volumes), about which it will quickly inform the FCA and the PRA.

30 The FSCS will determine the Scheme levies in accordance with the FCA's and PRA's rules so that it has sufficient funds to cover its management expenses and to identify, assess and pay out valid claims. Proposed levies will usually be announced by the FSCS around the beginning of each financial year. Interim levies may be necessary where matters are not fully known in time for the announcement of the main annual levy. The FCA and the PRA will discuss in advance, with each other and with the FSCS, whether the levy has or may have any significant effect on the market, a particular sector or individual firms and, where there is, what (if any) action might be reasonably practicable and appropriate to address that effect.

31 The FSCS will publish a statement of its policy on raising compensation cost levies, having taken into account the views of the PRA and stakeholders. If the FSCS amends the statement, it will follow the same process. The statement will include the policy on:

- raising annual compensation cost levies;
- raising interim compensation cost levies;
- estimating expected compensation costs;
- holding funds to meet expected compensation costs and refunding recoveries and other surpluses;
- raising compensation cost levies that are to be allocated to the retail pool; and
- borrowing, including borrowing from commercial sources, borrowing from the National Loans Fund, borrowing for short term liquidity purposes and borrowing for longer-term funding purposes.

32 The board of the FSCS is responsible for its treasury management policies, which cover the handling of cash balances and other invested funds. It will keep the PRA informed of these policies.

Co-ordination between the FCA and the PRA

33 As set out in the MoU between the FCA and the PRA¹, the CEOs along with the CEO of the FSCS will meet regularly to advise the boards in relation to their oversight of the FSCS and to ensure that any operational matters of mutual interest are addressed effectively.

¹ <http://www.bankofengland.co.uk/about/Documents/mous/moufcapra.pdf>

Reporting to the PRA

34 As required under FSMA, the board of the FSCS will report to the PRA (and FCA) on the discharge of its functions on an annual basis and will prepare and publish an Annual Report to support this. The report will be made within four months of the end of the financial year being reported on. The FSCS agrees to give reasonable time to allow the PRA to provide considered comments on drafts of its Annual Report and accounts.

35 The Annual Report will include:

- a statement regarding its finances as provided in the rules made by the PRA; and
- a statement or summary of transactions of the deposit and insurance provision scheme classes and, within the insurance provision class, the general and life sub-classes during the year.

36 In addition, if reasonably requested by the PRA, the FSCS will provide the PRA with interim reports, at such other intervals as may be agreed, in an agreed form. It may include a commentary on the FSCS's performance against its management plans and its budget together with information about its Scheme activities including the number of claims by type of business received, decisions taken and pay outs made.

37 The FSCS will also provide the PRA with any final reports produced by the National Audit Office prior to publication.

38 Under section 74 of the Financial Services Act 2012, there are circumstances in which the PRA must carry out an investigation and report on a possible regulatory failure. If requested, the FSCS will provide a comprehensive report to the PRA, setting out the facts and circumstances of its involvement, to aid the PRA's fulfilment of its statutory duty. The PRA may also request reports after pay outs or other failures.

Disaster recovery

39 The FSCS will keep the PRA informed about its disaster recovery arrangements that it would adopt in the event that its premises cannot be occupied. The FSCS will also notify the PRA as soon as possible if there is an event that leads to the arrangements being invoked.

Review of MOU

40 The Chief Executives of the PRA and the FSCS will review the operation of the MoU and the effectiveness of co-operation and co-ordination on an annual basis, consulting the head of the Bank's Special Resolution function as appropriate.