

## **FSCS Podcast - Episode 12 Mini-pod: What does FSCS mean when it declares a firm 'in default'?**

0:01 – Jess Spiers (Jingle)

Welcome to Protect Your Money with FSCS, the podcast from the Financial Services Compensation Scheme. Today we've got a mini-pod for you; a special bite sized episode where we talk through a particular topic to explain it all simply. In this series, we explain how we can help to protect your money so you can feel confident your money is safe. Let's get into the conversation now.

0:29 – Nigel Yeates

Welcome to this short episode of the FSCS podcast. I'm your host Nigel Yeates, Communications and Stakeholder Business Partner at FSCS. I'm joined today with my colleague, Simon Wilson, Head of Resolution at FSCS. Today we're explaining one of the often used but rarely understood FSCS terms. Simon, what do we mean when we say we've 'declared a firm in default'?

0:49 – Simon Wilson

To start with, I think it's worth saying that before compensation can be paid to customers of a failed authorised firm, the firm must be declared in default by FSCS. And this term 'declared in default' is very much an FSCS-specific term used to describe a firm which has essentially gone bust or become insolvent, which really means that it cannot pay claims, which are made against it.

1:12 – Nigel Yeates

That's right, and we try not to use 'in default' too often as we know most people won't know what it means, but sometimes we do need to use it. So next question then Simon, is the in default process the same for all types of firms?

1:25 – Simon Wilson

No, the process for declaring firms in default varies depending on the type of firms. So, for example, for failed deposit takers such as credit unions or building societies or insurance companies, the trigger for FSCS to declare these firms in default is usually a court order, which formally appoints Administrators or an Insolvency Practitioner to a firm which has become insolvent.

1:49 – Nigel Yeates

And what about advisors?

1:52 – Simon Wilson

For other authorised firms such as Independent Financial Advisors and other advising firms, three criteria need to be met before if FSCS can declare a firm in default. Firstly, FSCS must have received an eligible claim for compensation against a financial firm that's authorised by the Financial Conduct Authority or the Prudential Regulation Authority. And secondly, the claim must show that the customer has lost money in relation to a regulated activity carried out by the firm.

2:19 – Nigel Yeates

Could I just jump in here and ask - what do we mean by regulated activity?

2:24 – Simon Wilson

Sure, when we talk about regulated activities, these are the specific activities that an authorised firm is carrying out with its customers. Providing regulated financial advice is an example of a regulated activity. I think it's also worth mentioning that a firm must be regulated by the PRA, or the FCA for FSCS protection to apply. And we always encourage people to check on the firm's authorisation status by asking the firm. And back to your original question, the third and final criteria which needs to be met before FSCS can declare a firm in default, is that it must be shown that the firm itself cannot meet or pay claims against it.

3:05 – Nigel Yeates

Thanks very much, what else will be useful for our listeners to know about in default?

3:10 – Simon Wilson

For the most part, the claims FSCS receives or against firms, which have already been declared in default, but if we do receive a claim against the firm, which is yet to be declared in default, it is the receipt of this claim which will trigger a solvency investigation into the firm. And it's really this investigation, which will determine whether or not firms can pay claims themselves. In terms of submitting a claim, most customers use our online claim service and I always like to remind people that our service is completely free. And claiming online means that FSCS will also tell you straight away if you're eligible to make a claim.

3:47 – Nigel Yeates

Perfect, thank you and what else happens before the claims process begins?

3:52 – Simon Wilson

It's probably worthwhile saying that at this point, that FSCS only opens up and begins accepting claims if either the firm being claimed against has had its authorisation removed or where the firm has entered formal insolvency and customers are unable to submit claims to FSCS against firms which remain authorised and are still trading. In those cases, that's where the Financial Ombudsman Service can help - with issues where the firm is still 'live'.

4:18 – Nigel Yeates

Thanks, and what happens when you receive a claim against one of these firms?

4:21 – Simon Wilson

When we receive a claim for a firm not yet declared in default, we will notify the relevant person or firm of our investigation and request information from them about their ability to pay claims made against them. And if we don't receive this information, we will

assess their ability to pay potential claims against them after making enquiries using public sources.

4:44 – Nigel Yeates

Great, that's all clear. And what happens next?

4:47 – Simon Wilson

If following this assessment, we believe that the relevant person or firm is unable or likely to be unable to pay claims. We will notify them of our intention to declare them in default, allowing them some time to object. If, at any time, FSCS decides that the relevant person or firm can pay all claims against them, we will of course inform them and any claims against the person or firm would then be made directly to them.

5:14 – Nigel Yeates

Are these solvency investigations complex?

5:17 – Simon Wilson

It really depends on the company. The complexity of solvency investigations we carry out can vary based on the type of business being investigated. An example of a reasonably straightforward investigation would be an investigation into a limited liability company, which has entered formal insolvency such as Liquidation.

5:38 – Nigel Yeates

And that one is defined as reasonably straightforward because of what reasons?

5:42 Simon Wilson

Well, for these types of firm directors cannot be held personally liable or responsible for the limited company's debts and least they've signed personal guarantees. So, it's often the case that the firm's insolvency itself indicates that the firm cannot meet claims.

5:58 – Nigel Yeates

And what about for other types of businesses?

6:00 – Simon Wilson

Solvency investigations into sole traders or partnerships are different and sole traders, for example, have unlimited personal liability, which means they are personally accountable for their business' debts, including claims. The solvency investigations that we carry out under sole traders will examine the personal assets and liabilities of an individual before a decision is made to declare them in default or not.

6:25 – Nigel Yeates

Thanks. And do all these different scenarios require a lot of coordination with several other organisations?

6:31 – Simon Wilson

Yes, absolutely. It's extremely important that if FSCS works closely with our regulatory partners, such as the FCA and Financial Ombudsman Service to really understand as much as possible, about potential failures before they land with us. And it's this engagement which feeds into our operational planning and forecasting so that we are as prepared as possible for firm failures, meaning that we can respond and serve our customers as efficiently as possible.

7:00 – Nigel Yeates (Jingle)

Thanks so much for all that useful information, Simon. For our listeners, we've also got more information and background on our website [www.fscs.org.uk](http://www.fscs.org.uk). We hope everyone's enjoyed listening to this mini podcast. You can find all of our podcasts on our website, and the usual places you find your podcasts. We'd love to hear what you think so please do rate and review us and you can also let us know on our social channels. Just search for @FSCS. Thanks everyone for listening!