

Your World First

C/M/S/

Law . Tax

Living Wills in Outsourcing Arrangements



Living Wills in Outsourcing Arrangements

There have been many high profile, and countless other, examples of outsourcing firms struggling, or even failing, over the last few years. As a consequence of this and the growing complexity of business operations and reliance on technology, firms looking to outsource, or with arrangements already in place, are increasingly focusing on ensuring operational resilience and business continuity in connection with their outsourcing arrangements.

It is an area of significantly increased scrutiny in public sector outsourcings and, in the financial services sector, has become a key area of regulatory attention. On 5 December 2019, the FCA, PRA and Bank of England all published their joint and coordinated Consultation Papers on new requirements to strengthen operational resilience in the financial services sector. The consultations are, among other things, a response to the Treasury Select Committee's investigation into IT failures within the financial services industry.

Areas of focus include governance and supervision, outsourcing policies, concentration risks, security and data, risk assessments and supply chain due diligence. From a business continuity perspective stakeholders are also looking at termination and exit rights and arrangements – in both planned and distressed scenarios. For many outsourcing arrangements living wills can play a significant role in assisting customers to maintain operational resilience.



What is a Living Will?

The concept derives from the Government's response to the repercussions from the Carillion insolvency in 2018. In the context of a services arrangement the term is used to describe contingency planning and how the customer will respond in the event of a complete non-availability of or non-performance by their supplier, e.g. due to insolvency or an irretrievable service failure following a disaster.

Note that these types of plans are to be distinguished from recovery and resolution plans, which are also commonly referred to as "living wills". The recovery and resolution regime applies to Europe's biggest banks and was introduced in the Bank Recovery and Resolution Directive as implemented in the UK by the Banking Act 2009. A similar regime has been introduced in the USA. Bank recovery and resolution plans are self-assessments of all operational aspects of a bank and how it might be wound down or recovered in an orderly way in order to avoid future tax-payer bailouts. Interestingly proposals are afoot to extend this concept into the insurance sector ...

Firms wishing to work with the public sector on significant outsourcing arrangements should now expect to be required to provide and evidence greater transparency of their delivery models, a commitment that outsourcing will be a 'force for good' and to create living wills to facilitate contingency planning. This shift in policy was explained by Cabinet Office Minister, David Lidington, in a speech he is reported to have made at the Business Services Association:

"Carillion was a complex business and when it failed it was left to government to step in – and it did..."

"But we did not have the benefit of key organisational information that could have smoothed the management of the liquidation."

"By ensuring contingency plans can be put in place in the very rare event of supplier failure, we will be better prepared to maintain continuity of critical public services"

In the absence of a clear and current succession plan, the process of ensuring that the needs of all end users, clients and stakeholders were covered, took far longer than it should have done following Carillion's collapse.



What Does a Living Will Comprise?

A living will usually includes detailed customer contingency plans that describe all material aspects of running the contract. Ideally the plans will be updated at least every six months to ensure that the services from the supplier remain aligned to the customer's changing business operations, objectives and outcomes. The focus of the plans is to capture the information necessary to ensure that when the contract ends, whether a natural expiry or planned early termination or an unexpected or unwanted early end, the customer and/or one or more replacement providers can take over seamlessly to ensure that the customer's business operations suffer minimal disruption and its service users are not unduly inconvenienced.

Areas of focus include providing for a variety of fallback scenarios and making sure the necessary resources and information are available to facilitate their implementation:

- identifying and where appropriate engaging with one or more back up suppliers, and taking steps to ensure they have sufficient up-to-date knowledge of the outsourced function and associated services and delivery mechanics;
- maintaining incident management, business continuity and disaster recovery plans;
- regular systems and data access and backup;
- maintaining premises, personnel and asset records and registers;
- identifying subcontractor and supply chain contracts and relationships and taking steps to ensure they can be transferred or replaced where necessary; and
- taking steps to ensure adequate financial stability such as securing payment to subcontractors and other suppliers (throughout the supply chain).

These need to be backed up by appropriate provisions in the outsourcing contract (and often the subcontractor supply chain contracts).



Telltale Signs

There's no one size fits all guide to when a customer should look to invoke its living will arrangements, but the following types of warning signs may be an indicator something is going awry and needs to be investigated further (although it may be difficult to secure some of the information necessary to identify them):

- Reduction in key staff members assigned to the relationship
- Key supplier staff and subcontractor resources leaving in significant numbers
- Sustained/persistent reduction in service level performance or increased incident levels
- Lack of investment in new products and services
- Reluctance to innovate or collaborate
- Failure to win new customer contracts, non-renewal or loss of existing customer contracts
- Concerningly high levels of sub-contractor disputes
- Payment delays to subcontractors
- Fall in share price
- Regulatory investigation or enforcement action
- Significant third party litigation / disputes

Final Thoughts

The increasing regulatory scrutiny in the financial services sector will inevitably lead to further guidance around measures that firms should take to ensure operational resilience. We can expect to see that develop over time into what is considered 'best practice' more generally and as a consequence firms increasing their focus on scenario planning for unexpected events and supplier and service failures. In turn that will impact on the fallback and contingency measures firms put in place, and the terms of outsourcing contracts.

Key Contacts



Ian Stevens

Partner

T +44 20 7367 2597

E ian.stevens@cms-cmno.com



Alan Nelson

Partner

T +44 141 304 6006

E alan.nelson@cms-cmno.com



Angela Greenough

Partner

T +44 20 7367 2198

E angela.greenough@cms-cmno.com



Paul Edmondson

Partner

T +44 20 7367 2877

E paul.edmondson@cms-cmno.com

Regulators consult on Operational Resilience: A paradigm shift in the regulation of financial stability

On 5 December 2019, the FCA, PRA and Bank of England all published their joint and coordinated Consultation Papers (available [here](#), [here](#) and [here](#)) on new requirements to strengthen operational resilience in the financial services sector. They are a response to the Treasury Select Committee's investigation into IT failures within the financial services industry. (The report is available [here](#) and our commentary [here](#)).

Read the full article [here](#).

IT failures in the financial services sector – Treasury Committee Report

The House of Commons Treasury Committee has published its Report into IT failures in the financial services sector, following an almost year-long inquiry that began in November 2018. The inquiry was launched in response to a number of high-profile IT failures at banks and other financial institutions that reportedly affected large numbers of customers. The Treasury Committee examined the causes and consequences of IT failures in the financial services sector and what was being done by industry and the FCA, PRA and Bank of England to promote operational resilience, in light of the rise of digital banking services

Read the full article [here](#).



Law . Tax

Your free online legal information service.

A subscription service for legal articles
on a variety of topics delivered by email.

cms-lawnow.com

CMS Legal Services EEIG (CMS EEIG) is a European Economic Interest Grouping that coordinates an organisation of independent law firms. CMS EEIG provides no client services. Such services are solely provided by CMS EEIG's member firms in their respective jurisdictions. CMS EEIG and each of its member firms are separate and legally distinct entities, and no such entity has any authority to bind any other. CMS EEIG and each member firm are liable only for their own acts or omissions and not those of each other. The brand name "CMS" and the term "firm" are used to refer to some or all of the member firms or their offices.

CMS locations:

Aberdeen, Algiers, Amsterdam, Antwerp, Barcelona, Beijing, Belgrade, Berlin, Bogotá, Bratislava, Bristol, Brussels, Bucharest, Budapest, Casablanca, Cologne, Dubai, Duesseldorf, Edinburgh, Frankfurt, Funchal, Geneva, Glasgow, Hamburg, Hong Kong, Istanbul, Johannesburg, Kyiv, Leipzig, Lima, Lisbon, Ljubljana, London, Luanda, Luxembourg, Lyon, Madrid, Manchester, Mexico City, Milan, Mombasa, Monaco, Moscow, Munich, Muscat, Nairobi, Paris, Podgorica, Poznan, Prague, Reading, Rio de Janeiro, Riyadh, Rome, Santiago de Chile, Sarajevo, Seville, Shanghai, Sheffield, Singapore, Skopje, Sofia, Strasbourg, Stuttgart, Tirana, Utrecht, Vienna, Warsaw, Zagreb and Zurich.

cms.law

UK-634683015.1

December 2019