



Securities Industry Association



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Statement of

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***Testifying on Behalf of
The Bond Market Association
and Securities Industry Association***

***Chairwoman Sue W. Kelly
House Financial Services Subcommittee on Oversight and Investigations
U.S. House of Representatives***

***Hearing on Pandemic Influenza Preparedness in the Financial Services
Sector***

I am Gregory J. Ferris, Managing Director of Global Business Continuity Planning at Morgan Stanley. I am also Chairman of the Securities Industry Association Business Continuity Planning Committee. Today I am testifying on behalf of the Bond Market Association (BMA) and the Securities Industry Association (SIA). I am grateful for the opportunity to testify on steps taken by our member firms to prepare for a pandemic. The members of these two organizations welcome and thank you for your leadership on this issue.¹

Securities firms and banks take business continuity planning (BCP) seriously and have committed significant time and financial resources to the effort. Even before the September 11, 2001 terrorist attacks on New York and Washington, the industry was

¹ The Bond Market Association represents securities firms, banks and asset managers that underwrite, invest, trade and sell debt securities in the \$46 trillion global bond markets. The Securities Industry Association brings together the shared interests of more than 600 securities firms including investment banks, broker-dealers, and mutual fund companies. The U.S. securities industry manages the accounts of nearly 93 million investors directly and indirectly through corporate, thrift, and pension plans.

developing business continuity strategies in anticipation of business-interrupting events, both natural and man-made. The September 11 attacks highlighted serious weaknesses in the area of firm communications. The industry began identifying and addressing these problems immediately. We learned a great deal from that experience and worked closely with federal regulators and the self-regulatory organizations to craft effective rules and practices for business continuity planning. The results of this work have been positive and visible. Lessons learned on September 11 helped form the foundation on which the industry-wide Command Center Structure was built. Recovery efforts following the 2003 New York City blackout and other events, such as the 2005 transit strike and national immigration rallies, were more effective because this structure was in place.

The Intelligence Reform and Terrorist Prevention Act of 2004 required the federal financial regulators to produce a joint report on the efforts of the financial sector to implement recommendations of the Interagency White Paper, *Sound Practices to Strengthen the Resilience of the U.S. Financial System*.² As you know, that report found that firms have substantially implemented the interagency recommendations, which include the creation of geographically diverse backup sites for critical functions.

Instead of damaging physical infrastructure, a pandemic would affect financial sector workers by limiting their ability or willingness to report to work. Traditional backup strategies that rely on remote facilities might not be effective in this case since it is likely that employees in many different geographic areas would be affected simultaneously. In more advanced pandemic scenarios, many individuals may have to work from home or dispersed locations rather than centralized backup facilities. Some firms with a global reach began actively addressing the pandemic issue during the SARS outbreak in 2003. Since then, firms of all sizes, in conjunction with the Federal Financial Institutions Examination Council, have begun to focus on the question. The national and local government public health response to a pandemic could include bans on non-essential travel and severely limit public activity for periods of weeks. Faced with these challenges, securities firms of all sizes began studying the issues and designing and implementing response strategies over a year ago.

Under a pandemic scenario, new questions are raised that can generally be categorized as either prevention or recovery. Prevention refers to limiting the effects of the pandemic on the work force in advance of an outbreak. Recovery focuses on business continuity, or how to maintain business operations as efficiently as possible once an outbreak occurs. Prevention-focused questions include how much medicine to stockpile and what type of hygienic supplies, such as surgical masks, should be kept on hand. The answers to other questions are contingent on government responses. If there are travel bans, school and day care center closures, and commuting is curtailed, firms will need to understand how they can operate remotely, with the majority of employees working from home.

To ensure continuity of business, the industry has begun taking dramatic steps to ensure that individual firms, exchanges and industry utilities remain open and that the financial markets continue to operate effectively. The resulting response strategies consider the

² Securities Exchange Act Release No. 47638 (April 7, 2003), 68 FR 17809 (April 11, 2003)

following questions, among others: What functions can be performed from home and what functions will require employee presence at a centralized facility? Does the firm have sufficient online, or bandwidth, capacity? Is the remotely accessed computer system sufficiently secure?

The industry must also consider the aggregate effect of so much bandwidth utilization in a relatively confined geographical region. The usefulness of remote computing is limited if the available telecommunications infrastructure cannot adequately handle a sudden spike in activity. The sluggish system response during the 2005 New York transit strike provided an indication we can expect problems in this area.

A critical determinant of how the industry will ultimately respond to a pandemic is inextricably linked to the ability of the telecommunication infrastructure to meet the surge in demand associated with a pandemic. While this is not something the financial industry can directly control or manage, we are working closely with the telecommunications sector to address mutual issues of concern.

Industry Preparation Efforts

The BMA and SIA began addressing the possibility of a pandemic almost two years ago. Efforts are focused on four fronts: 1) information sharing; 2) strategies and practices; 3) emergency coordination; and 4) regulatory coordination.

Business Continuity Planning Committees: The BCP Committees of both associations, which are comprised of representatives of securities firms and other industry organizations and Association staffs, have worked together on the pandemic issue and have established special working groups to focus specifically on preparation and response. Committees dedicate meetings to reviewing various response strategies and both Associations make relevant information available via the Internet. While targeted to association members, these websites are public.

Securities Industry Command Center Structure: The Command Center Structure refers to a communication arrangement between the SIA Command Center, the BMA Command Center, federal regulators, self-regulatory organizations, the Financial Services Sector Coordinating Council, public sector emergency management organizations and others.³ Working together, these command centers coordinate industry response to significant events affecting the securities industry. The command centers serve as focal points for information and response decisions. Physical and virtual facilities, communication links, and contact lists are all in place. The command center procedures have been modified to more effectively coordinate response to a pandemic.

Pandemic Scenario Exercise: This week the BMA and the SIA conducted a joint exercise focused on pandemic response issues involving 14 of the largest securities firms. This forum provided an opportunity for firms to highlight the most effective response

³ Key Command Center participants include, in addition to the Associations, the New York City and New Jersey Offices of the Emergency Management (OEM) and the Federal Reserve Bank of New York.

strategies, identify remaining challenges and discuss open issues. The firms were presented with an escalating pandemic scenario that focused attention on issues that would likely affect the operation of the financial markets. Participants were asked how they would respond to the changing situations.

The exercise was intended to provide insight into the circumstances under which firms would operate and to determine what regulatory leeway may be required to ensure the continued efficient operation of the financial markets. Preparations discussed for an early-stage pandemic included routine preventative measures such as stockpiling hygienic supplies and preparing educational programs. In more advanced stages, firms' proposed operating procedures became less certain and based on assumptions that the telecommunications and clearing infrastructure would continue to function. The Depository Trust Clearing Corporation (DTCC) assured participants the clearing process would continue to operate even in the event of an advanced-stage pandemic, with a 60 percent employee absentee rate. The ability of the telecommunications system to handle a sudden spike in Internet demand in a specific geographic region with a concentration of securities industry workers simultaneously seeking network access is less clear at this point. The SIA and the BMA plan to form a working group with telecommunications industry representatives soon to better understand this situation.

Officials from the Securities and Exchange Commission (SEC), the Department of the Treasury, the Commodity Futures Exchange Commission (CFTC), the Federal Reserve Board, the Federal Reserve Bank of New York, the National Association of Securities Dealers, the New York Stock Exchange, the Clearing Corporation and the DTCC all observed the exercise. An SEC official suggested the agency meet directly with the Associations' BCP committee members to further the discussion of pandemic preparedness. A dominant question in the exercise was how regulators would react in a crisis. While exercise participants agreed regulators have been responsive and understanding in past emergencies, there remains a concern that regulators across all markets act consistently.

Industry Directory Utility: During a pandemic, a significant percentage of securities industry personnel could be required to work from home or another remote location for an extended period of time. Communications between firms and other industry participants will be difficult for many reasons. Indeed, even identifying the staff responsible for various functions could prove to be an enormous challenge. The BMA and the SIA are exploring the possibility of creating an Industry Directory Utility (IDU) to facilitate better communication during a pandemic.

The IDU would serve as a secure, industry-wide repository of contact information both for individuals and functions at participating firms and other organizations. This would facilitate the ability of employees to communicate with each other in order to trade, sell, clear and settle securities transactions and to conduct related fundamental business activities and responsibilities in the interest of fostering the confidence of investors.

Several firms and regulatory agencies have expressed interest in the concept. The Associations are working to determine the extent of firm participation as well as funding sources. The Associations are also taking up questions of IDU structure, security and regulatory and internal control implications.

Regulation

A pandemic has the potential to severely damage the operation of the financial markets. With careful study and planning, however, the SIA and the BMA are confident the markets can continue to function smoothly. It is likely, however, that some regulatory flexibility will be required. Indeed, Congress and the financial regulators have contemplated this question. Under the Terrorism Prevention Act, the SEC is granted emergency powers—in consultation with the Federal Reserve Board, the Treasury Department and the CFTC—to alter or suspend any securities regulation, including those of self-regulatory organizations.

Precisely which areas of regulation are most likely to require flexibility is not completely known at this point. The SIA and the BMA are encouraged by the pro-active focus of regulators. In May, the New York Stock Exchange released a memo describing the types of regulatory latitude the exchange is likely to consider, including delays in real-time supervision where technology monitoring is feasible and additional time for reconciliations. This represents the sort of flexibility the industry will require to assure the financial markets can continue to operate without interruption in the event of a pandemic.

Regulators have challenged the industry in an appropriate way to put in place effective BCP plans. We welcome a continued constructive dialogue and specific guidance.

Conclusion

The terrorist attacks of September 11, the SARS outbreak in 2003, and current pandemic concerns all highlight the obligation the members of the SIA and the BMA have to ensure, to the best of their ability, that financial markets remain open and efficient during periods of emergencies. The associations and their members have committed significant resources to meet this obligation. Collectively, and with the assistance of our regulators, we have made great progress. Some substantial concerns remain, however, which we are committed to addressing.

Although no one can say with any certainty when and where the next pandemic will occur, or how serious it will be, medical experts around the globe believe we are closer to that point than any other time since the last pandemic in 1968. An infectious disease outbreak will challenge our industry and the global economy like no other event. It will know no borders, and many of the solutions that we typically bring to bear to resolve problems will not be effective. We must continue to work independently, with our industry and the medical community and governments around the globe, to develop creative solutions to this unique challenge.

Thank you again Chairwoman Kelly for your interest in this important issue and the opportunity to testify today.