


Individual Accountability: Extending the Senior Managers and Certification Regime to all FCA firms

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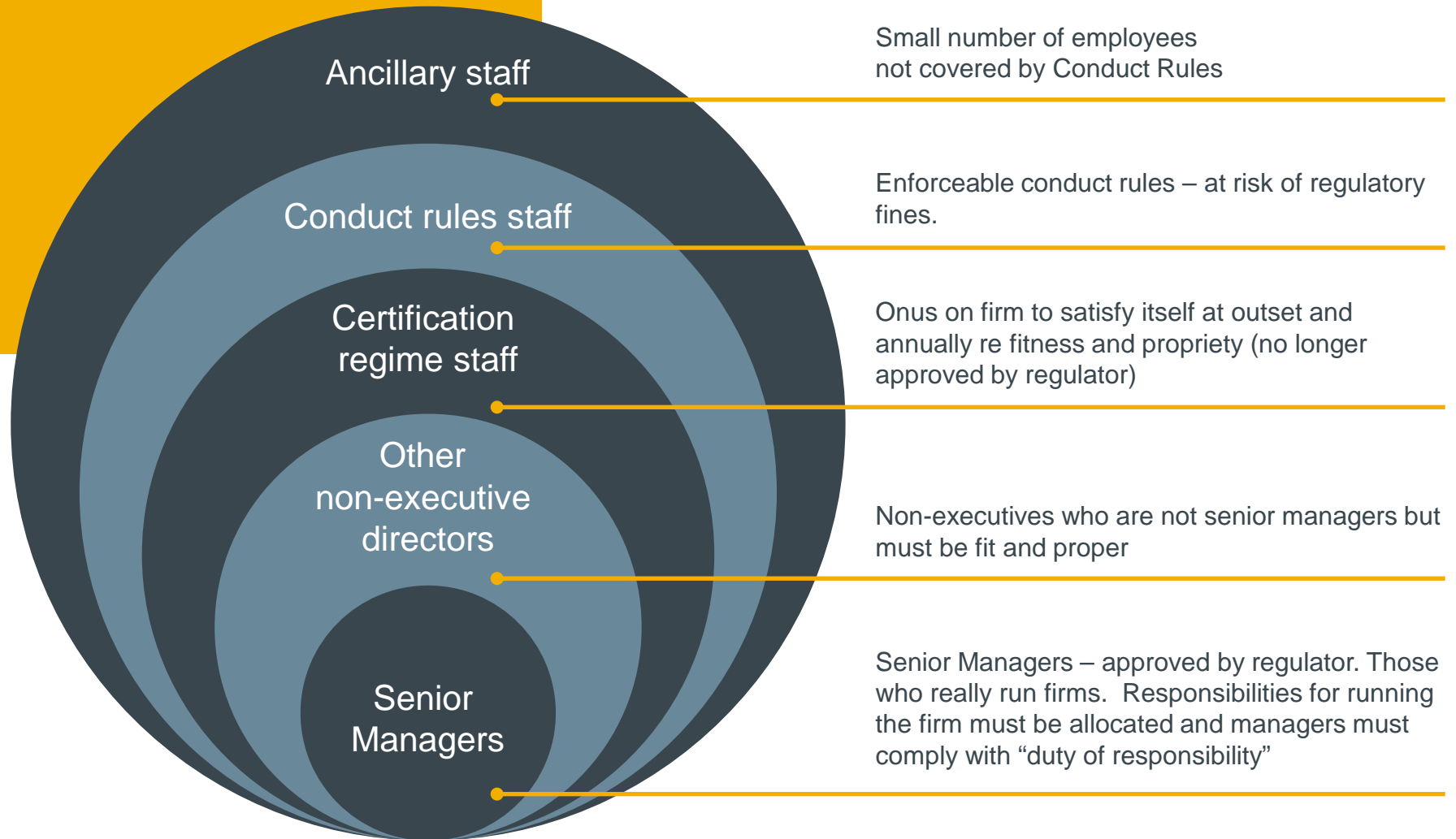
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“Just before the new accountability regime was introduced, I was at an event debating the concept of responsibility – with many arguing that it is a difficult thing to define. A young lady stood up and said that she didn’t know what all the fuss was about – she was teaching her children to take responsibility for their actions – so why should people who work in financial services be any different?”

*Andrew Bailey – Chief Executive of
the Financial Conduct Authority
The Guardian – 27 Sep 2016*

SM&CR: what is the new regime?



Overview

New regime focussed on individual accountability

- Individuals currently engaged to carry out controlled functions on behalf of UK authorised entity must be pre-approved by the Financial Conduct Authority
- The “approved persons” regime involves a process of approval when on-boarding staff into a controlled function role and processes for notifications to the FCA in relation to changes
- From March 2016, banks, building societies and credit unions (including branches of overseas firms) have been subject to a new regime – the Senior Managers and Certification Regime
- From the same date, insurance firms have been subject to the Senior Insurance Managers regime (a lighter touch version) – extension being separately consulted on
- Consultation on extension to all authorised firms now launched – closes 3 November 2017
- Policy Statement / Final Rules, Summer 2018
- Will be implemented “from 2018”
- The new regimes focus on:
 - Individual accountability at the most senior levels and approval of senior managers by the regulator
 - Ongoing responsibility on firms for the fitness and propriety of their senior managers and certified population
 - Individual conduct obligations (enforceable conduct rules)
 - Some overlap with governance requirements of MiFID2
- Firms divided into Core, Limited Scope and Enhanced

All FCA solo-regulated firms

1 Limited Scope

Currently have limited application of Approved Person regime, including:

- Limited permission consumer credit firms
- Sole traders
- Authorised professional firms - non-mainstream regulated activities
- Oil market participants, service companies, energy market participants
- Insurance intermediaries whose principal business is not insurance intermediation and who only have permission to carry on insurance mediation activity in relation to non-investment insurance contracts
- Internally managed AIFs

2 Core

All other FCA solo-regulated firms

3 Enhanced

- Significant IFPRU
- CASS Large Firm
- AUM £50 billion or more
- Total intermediary regulated business revenue of £35 million or more
- Annual regulated revenue generated by consumer credit lending of £100 million or more
- Mortgage lender with 10000 or more regulated mortgages outstanding

Key elements (Senior Managers): Core vs Enhanced vs Limited Scope

1 Core	2 Enhanced Firms	3 Limited Scope
<ul style="list-style-type: none"> • Senior Management Functions • Duty of Responsibility • Statements of Responsibilities • Criminal Records Checks • Prescribed Responsibilities 	<p>As for Core but add:</p> <ul style="list-style-type: none"> • Additional Senior Management Functions • Additional Prescribed Responsibilities • Responsibilities Map • Handover Procedures • Overall Responsibility 	<p>As Core but add:</p> <ul style="list-style-type: none"> • SMF 29 Limited Scope Function - for certain Limited Scope firms <p>And minus:</p> <ul style="list-style-type: none"> • Prescribed Responsibilities

Senior manager functions: **Core Regime**

Governing functions		Existing FCA CF?
SMF1	Chief executive	CF3
SMF3	Executive director	CF1
SMF27	Partner	CF4
Governing functions: non-executive		
SMF9	Chair	Note most CF2s (NEDS) will no longer be approved
Required functions		
SMF16	Compliance Oversight	CF10
SMF17	MLRO	CF11
SMF29	Limited scope function	CF8

Senior manager functions: **Enhanced Regime**

Functions		Existing FCA CF?
SMF2	Chief finance function	CF28?
SMF4	Chief risk function	
SMF5	Head of internal audit	
SMF14	Senior independent director	CF2?
SMF12	Chair of the remuneration committee	
SMF10	Chair of the risk committee	
SMF11	Chair of the audit committee	
SMF13	Chair of the nominations committee	
SMF7	Group entity senior manager function	CF29?
SMF24	Chief operations function	NEW
SMF18	Other overall responsibility	CF29?

List of prescribed responsibilities

Core

1	Performance by the firm of its obligations under the Senior Managers Regime, including implementation and oversight
2	Performance by the firm of its obligations under the Certification Regime
3	Performance by the firm of its obligations in respect of notifications and training of the Conduct Rules
4	Responsibility for the firm's policies and procedures for countering the risk that the firm might be used to further financial crime
5	Responsibility for the firm's compliance with CASS (if applicable)
6	Responsibility for ensuring the governing body is informed of its legal and regulatory obligations
7	Responsibility for an AFM's value for money assessments, independent director representation and acting in investors' best interests *Added as per the FCA's Asset Management Market Study

Enhanced

8	Compliance with the rules relating to the firm's Responsibilities Map
9	Safeguarding and overseeing the independence and performance of the internal audit function
10	Safeguarding and overseeing the independence and performance of the compliance function
11	Safeguarding and overseeing the independence and performance of the risk function
12	If the firm outsources the internal audit function, taking reasonable steps to ensure that every person involved in the performance of the service is independent from the persons who perform external audit
13	Developing and maintaining the firm's business model
14	Managing the firm's internal stress tests and ensuring the accuracy and timeliness of information provided to the FCA for the purposes of stress testing

New regimes

1 Senior managers

- Largely aligned with SIF population
- Annual assessment of fitness and propriety
- Approved by FCA
- Statement of Responsibilities
- Allocation of ‘prescribed responsibilities’
- Formal duty of responsibility to take reasonable steps to prevent breaches

Enhanced Only

- Management responsibilities map
- Formalised handover

Territorial scope (other than branches):

No territorial limitation

2 Certification staff

- Largely aligned with existing (non-SIF) approved population – although NB. CF29
- No central register and no approval process
- Firms take responsibility for assessing fitness and propriety and re-confirming this on an annual basis
- Brings in MRTs
- Increased focus on regulatory references and processes for assessing fitness and propriety for staff on an on-going basis

Territorial scope (other than branches):

People based in the UK or if based outside the UK are dealing with UK clients

3 “Enforceable” conduct rules

- Most staff working for regulated entities will be covered
- Rules largely reflect existing rules for approved persons
 - Positive duty to report on senior managers
 - All conduct rules staff have a duty to treat customers fairly
- Firms are required to report breaches to the regulator
- Findings of breach of conduct rules to be included in regulatory references
- Conduct rules staff at risk of direct regulatory enforcement/ fines

Territorial scope (other than branches):

All staff of UK firm (except ancillary staff) in relation to financial services activities

Certification Regime

Certification Regime

Those who could cause significant harm, might include

- Significant management function (based on current CF29)
- Material Risk Takers
- Algorithmic trading
- Most former Approved Persons not covered by SMR
- Customer-facing roles with a required qualification
- Proprietary traders
- CASS Oversight
- Line Managers of Certified People
- Current CF30s (i.e. customer-dealing function)

Conduct Rules

Senior managers, certification staff and most other staff (other than limited ancillary staff)

New Conduct Rules - Second Tier



Senior Manager Conduct Rules

- SM1: You must take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively
- SM2: You must take reasonable steps to ensure that the business of the firm for which you are responsible complies with relevant requirements and standards of the regulatory system
- SM3: You must take reasonable steps to ensure that any delegation of your responsibilities is to an appropriate person and that you oversee the discharge of the delegated responsibility effectively
- SM4: You must disclose appropriately any information of which the FCA or PRA would reasonably expect notice

New Conduct Rules - First Tier



Individual Conduct Rules

- Rule 1: You must act with integrity
- Rule 2: You must act with due skill, care and diligence
- Rule 3: You must be open and cooperative with the FCA, the PRA and other regulators
- Rule 4: You must pay due regard to the interests of customers and treat them fairly
- Rule 5: You must observe proper standards of market conduct

Proportionality

FCA emphasis on the principles of proportionality, simplicity and flexibility

- FCA do not expect firms to change how they organise themselves or to hire people to fill specific functions
- Aim of the regime to “clarify and reinforce whatever governance structures firms choose to have in place”
- However:
 - When considering the new senior management functions, the FCA recommends firms should think about the new responsibilities that it expects firms to allocate among its senior managers
 - Need to align HR processes with new requirements (e.g. annual assessment, regulatory references)
 - “Tone from the top” is key/early communication/fitting the firm’s culture and using implementation positively to be clear on roles and responsibilities/delegation/processes
 - Update templates, handbooks and policies

Incoming UK branches

1 UK Branch of EEA firm

- Senior managers:
SMF 21: EEA branch senior manager
SMF 17: MLRO
- Certification regime: Applies to people based in the UK but not people based outside the UK even if they deal with a UK client
- Conduct rules: all staff based in the UK (except ancillary staff) in relation to financial services activities

2 UK branch of non-EEA firm

- Senior managers:
SMF 19: Head of Third Country Branch
SMF 3: Executive Director
SMF 27: Partner
SMF 16: Compliance
SMF 17: MLRO
- Certification regime: Applies to people based in the UK but not people based outside the UK even if they deal with a UK client
- Conduct rules: all staff based in the UK (except ancillary staff) in relation to financial services activities

Individual accountability for SMRs – what it means

Duty of responsibility – building on existing guidance and enforcement actions

- Concept of a Duty of Responsibility – extended in the same way as the Banking regime (PS17/9)
- Every Senior Manager has a duty of responsibility – SMs will be responsible for a breach in the area for which they are accountable unless they are able to demonstrate ‘reasonable steps’
- Burden of proof lies with the FCA to show that the Senior Manager did not take reasonable steps
- Criteria to be considered when taking action against Senior Managers
- Drives focus on individual accountability, better behaviour, ‘tone from the top’
- In practice what does this mean?
 - Focus on Statements of Responsibility
 - Reviewing and assessing risk in business areas
 - Reporting processes
 - Handover and due diligence
 - Expert advice
 - Protection (D&O policies, resource, record-keeping)
- No Final Notices on Senior Manager cases yet
- Standards will not be applied retrospectively or with the benefit of hindsight

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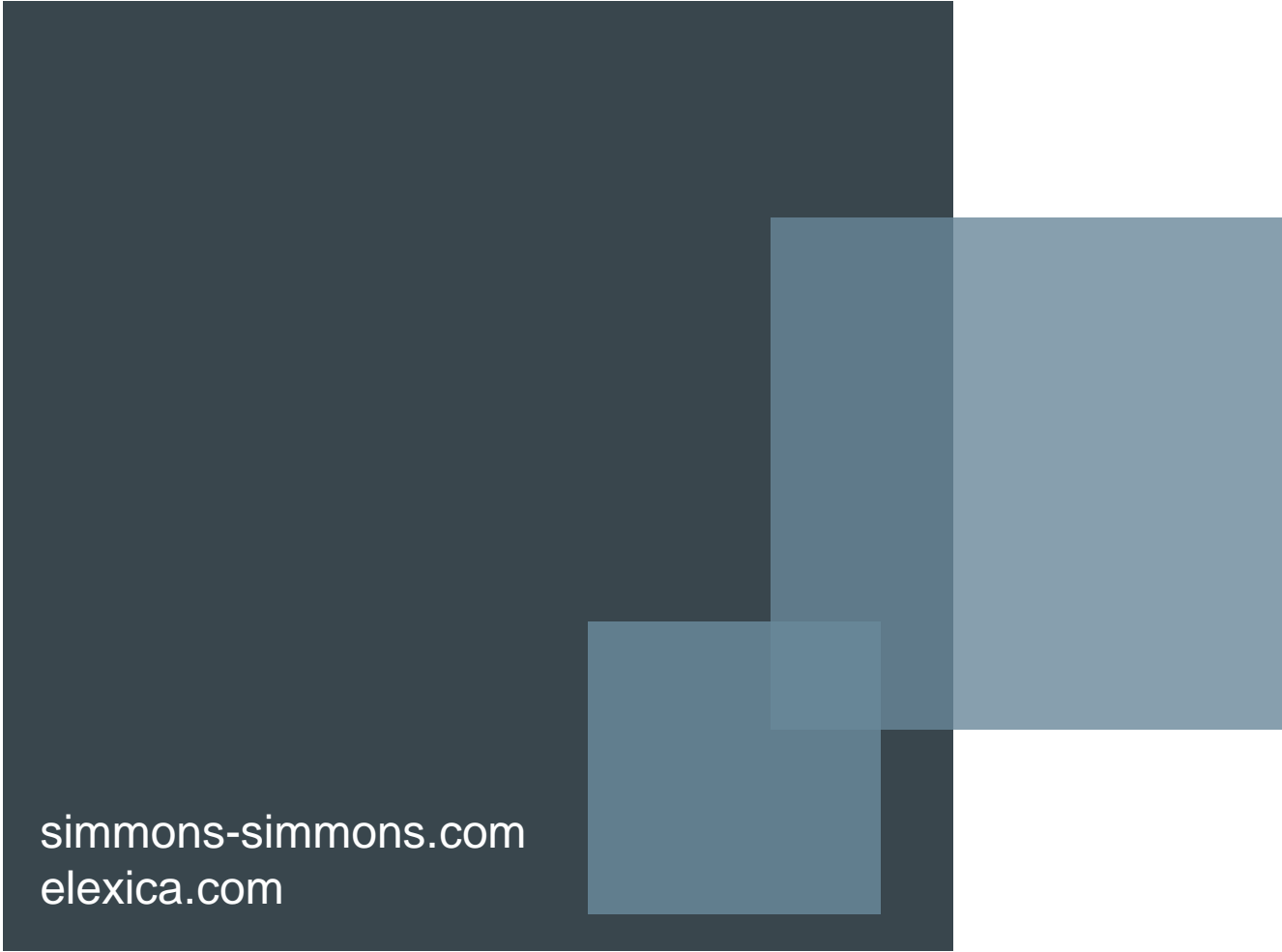
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