

FINANCIAL SERVICES

THE EXTENSION OF THE SENIOR MANAGERS AND CERTIFICATION REGIME TO FCA SOLO-REGULATED FIRMS

JULY 2019

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The extension of the existing Senior Managers and Certification Regime (SM&CR) initially put in place for Banks and Insurers was first proposed by Her Majesty's Treasury (HMT) in October 2015. It is set to replace the current Approved Persons Regime (APR) as from 9 December 2019 for all FCA solo-regulated firms.

In July 2018 the FCA published its near final rules on the extension of the SM&CR to all FCA solo-regulated firms authorised under the Financial Services and Markets Act 2000 (FSMA). These rules cover all firms regulated by the FCA and will apply to both firms and individuals performing financial services roles. The regime has been designed to be proportionate to firms' size and type of regulated activities.

The objectives of the new regime are reducing harm to consumers and strengthening market integrity by making individuals more accountable for their conduct and competence.

WHAT ARE KEY DIFFERENCES BETWEEN THE EXISTING AND NEW REGIME?

With individual accountability and having a healthy culture being key drivers for the FCA, the key differences between the new SM&CR and the outgoing APR are:

- ▶ the current APR will disappear for most firms (excluding Appointed Representatives and Payment Services firms) and be replaced by the Senior Managers Regime for the highest-ranking management;
- ▶ Senior Managers will be created and they will have clearer individual responsibilities and accountability;
- ▶ there will be a new Duty of Responsibility for Senior Managers, making them more accountable for regulatory contraventions in the part of the business for which they are responsible;

- ▶ firms will take over the responsibility for the certification (and assessing suitability, fitness and propriety) of certain individuals, from the FCA; and
- ▶ the new 'simple' Code of Conduct Rules will apply to almost everyone in the firm.

AN OUTLINE OF THE NEW REGIME

The regime classifies firms into three categories based on the firm's type and size – Limited, Core and Enhanced.

The three main elements of the original regime, as implemented for banking firms, remain and are called the 'Core regime' which will now apply to almost all firms. There are increased obligations for firms covered by the 'Enhanced regime' (larger and more complex firms), and reduced obligations for firms covered by the 'Limited scope' regime.

ELEMENT COMPRISING

Senior Managers Regime	<p>The most senior people in a firm will be approved by the FCA, with firms also having a responsibility to ensure these individuals are suitable and competent (fit and proper) to conduct their role (with firms reviewing this at least once a year). The Senior Managers will be required to have:</p> <ul style="list-style-type: none"> ▶ a Statement of Responsibilities – mapping what they are responsible and accountable for; ▶ a Duty of Responsibility – meaning that if something goes wrong in an area they are responsible for, the FCA will consider if they took 'reasonable steps' to stop it from occurring; and ▶ Prescribed Responsibilities – specific responsibilities that the FCA will require firms to allocate to their Senior Managers.
Certification Regime	<p>This covers employees who are not Senior Managers, but who can have a significant impact on customers, markets or the firm ('significant harm functions'). The roles include:</p> <ul style="list-style-type: none"> ▶ significant management function; ▶ proprietary traders; ▶ the CASS oversight function; ▶ functions subject to qualification requirements; ▶ client dealing functions; ▶ algorithmic traders; ▶ material risk takers; and ▶ any supervisor or manager of someone who is a certified person. <p>These individuals will not be approved by the FCA, but will need to be approved internally by their own firm. The firm will have to certify they are suitable (fit and proper) to carry out their job (with a review taking place at least once a year).</p>
Conduct Rules	<p>The Conduct Rules are split into two tiers.</p> <p>The first tier contains five Conduct Rules which apply to all staff with the exception of ancillary staff.</p> <p>There are four additional Conduct Rules which apply to Senior Managers only.</p> <p>There is a notification requirement to report breaches of the Conduct Rules.</p>

SENIOR MANAGER FUNCTIONS

Core, Enhanced and Limited regime firm (excluding branches) are required to have the following Senior Manager Functions (SMFs), as relevant:

SMF	CORE	ENHANCED	LIMITED
SMF1 – Chief Executive	X	X	
SMF10 – Chair of the Risk Committee		X	
SMF11 – Chair of the Audit Committee		X	
SMF12 – Chair of the Remuneration Committee		X	
SMF13 – Chair of the Nomination Committee		X	
SMF14 – Senior Independent Director		X	
SMF16 – Compliance Oversight	X	X	X
SMF17 – MLRO	X	X	X
SMF18 – Other Overall Responsibility		X	
SMF2 – Chief Finance Officer		X	
SMF24 – Chief Operations		X	
SMF27 – Partner	X	X	
SMF3 – Executive Director	X	X	
SMF4 – Chief Risk Officer		X	
SMF5 – Head of Internal Audit		X	
SMF7 – Group Entity Senior Manager		X	
SMF9 – Chair	X	X	
SMF29 - Limited Scope			X

PRESCRIBED RESPONSIBILITIES

Core and Enhanced regime firms will also have to allocate Prescribed Responsibilities to Senior Managers including those listed below. Limited scope firms will not be subject to this requirement.

Core firms have a minimum of 4 Prescribed Responsibilities to assign, with another possible 2 Prescribed Responsibilities, dependent on their activities, which are detailed below:

- ▶ performance of obligations under the Senior Manager Regime (including implementation and oversight);
- ▶ performance of obligations under the Certification Regime;
- ▶ performance of the firm in relation to notifications and training on the Conduct Rules;
- ▶ firm's policies and procedures regarding countering the risk of the firm being used for financial crime;
- ▶ firm's compliance with CASS (as applicable); and
- ▶ value for money assessments, independent director representation and acting in investors' best interests (Authorised Fund Managers only).

In addition to those listed above, Enhanced firms have a further 7 Prescribed Responsibilities which will need to be assigned to Senior Managers.

DUTY OF RESPONSIBILITY AND REASONABLE STEPS

Under the SM&CR the Duty of Responsibility applies to all Senior Managers and specifies the circumstances under which the FCA is able to take action against a Senior Manager. The burden of proof is on the FCA to demonstrate that the Senior Manager did not take reasonable steps to avoid a misconduct occurring or continuing in their area of responsibility. This links into a Senior Manager's Statements of Responsibility and it is important for Senior Managers to take reasonable steps to have effective oversight of the areas they are responsible for.

REGULATORY REFERENCES

The regulatory references obligation contained in the SM&CR requires firms to request references from past employers, and also to provide such references. This is a step up from previous referencing obligations and requirements, and enables firms to get the information they need to assist in assessing suitability and fitness and propriety of individuals. It applies to Senior Managers, Certification staff and non-approved NED roles.

ENHANCED REGIME FIRMS

As Enhanced regime firms are considered to be some of the largest and most complex that the FCA regulate, they will be subject to extra requirements. These include:

- ▶ more Senior Manager functions;
- ▶ more Prescribed Responsibilities for those Senior Managers;
- ▶ creating a full management responsibilities map for their business (setting out the firm's management and governance arrangements);
- ▶ design and implement full handover procedures (ensuring every Senior Manager role has the information and materials needed to do the job effectively); and
- ▶ ensure that there is a Senior Manager responsible for every area of their business (overall responsibility).

SO WHEN DOES THE SM&CR TAKE EFFECT?

The SM&CR takes effect in stages as follows:


COMMENCEMENT
9 DECEMBER 2019

Conduct Rules will apply to Senior Managers and Certification staff, thus prior to commencement firms must at least:

- ▶ identify Senior Managers and Certification staff;
- ▶ provide tailored training on the Conduct Rules; and
- ▶ review and update contracts of employment.


TRANSITIONAL PERIOD
9 DECEMBER 2019 –
8 DECEMBER 2020

During the one transitional year period, firms must:

- ▶ provide tailored training to all other Conduct Rules staff in preparation for when it applies to them on 9 December 2020;
- ▶ assess existing Certification staff for suitability;
- ▶ identify and assess any new Certification staff for suitability; and
- ▶ check that the firm's information is correct on the financial services register after automatic conversion.


POST TRANSITIONAL PERIOD
9 DECEMBER 2020

During the post transitional period, firms must:

- ▶ ensure the Conduct Rules are being complied with by all relevant staff;
- ▶ complete initial certification assessments; and
- ▶ ongoing requirements to train new staff in the Conduct Rules and to re-certify Certification staff as fit and proper at least annually.



HOW CONVERSION TO SENIOR MANAGERS IS GOING TO WORK

For Core firms, individuals will be automatically converted into a possible Senior Management function where they already hold a corresponding controlled function, potentially requiring little or no action from firms. For existing approved persons there is no need for firms to perform any extra checks (such as mandatory criminal records checks and regulatory references) because firms should already

being ensuring that these individuals are, and continue to be, fit and proper by performing such checks.

The one exception to the automatic conversion rule is for the individual who will be performing the Chair function (SMF9). In this instance the firm must notify the FCA which CF2 Non-executive director or CF1 Executive director will be the SMF9 using Form K.

For Enhanced firms, there will be no automatic conversion to Senior Manager roles. To convert existing controlled functions to the Senior Manager functions, Enhanced firms will need to submit a Form K conversion notification for each Senior Manager function together with Statements of Responsibilities and the firm's Responsibilities Map.

NEXT STEPS FOR FIRMS

Firms now have less than six months to prepare for implementation of the new regime and you need to start those preparations now.

Firms will need to consider:

AREA	CONSIDERATIONS	
Project planning	What firm type are you? Core, enhanced or limited scope?	<input type="checkbox"/>
	Who is planning and running your preparations?	<input type="checkbox"/>
	Who needs to be engaged in the project?	<input type="checkbox"/>
	Do you have a project plan?	<input type="checkbox"/>
Consider preparing a responsibilities map. Whilst only Enhanced firms are required to produce a full responsibilities map, this is a good exercise for all firms to carry out as it will assist in the transition to SM&CR.		
Senior Managers	Who are your Senior Managers going to be?	<input type="checkbox"/>
	Are they fit and proper?	<input type="checkbox"/>
	What will their responsibilities be?	<input type="checkbox"/>
	Are the allocated prescribed responsibilities clearly included in their statement of responsibilities?	<input type="checkbox"/>
	Are all prescribed responsibilities which apply to your firm covered?	<input type="checkbox"/>
	Are the current approved person functions correct to ensure easy conversion to Senior Manager functions?	<input type="checkbox"/>
	Do the Senior Managers need training on the duty of responsibility and the conduct rules?	<input type="checkbox"/>
	Do the Senior Managers understand and accept their statement of responsibilities?	<input type="checkbox"/>
	Which (if any) of the certification functions apply to your firm?	<input type="checkbox"/>



AREA	CONSIDERATIONS	
Certification	Have you identified our certified persons before commencement?	<input type="checkbox"/>
	Are they fit and proper now?	<input type="checkbox"/>
	How will you assess their ongoing fitness and propriety and integrate or embed these into existing HR processes?	<input type="checkbox"/>
	What training do you need to provide?	<input type="checkbox"/>
Conduct Rules	Who will the rules cover?	<input type="checkbox"/>
	How will training be tailored to different staff and how will this be done in the future?	<input type="checkbox"/>
	How are the notification requirements embedded into your HR processes?	<input type="checkbox"/>
Enhanced firms	How are you going to address the handover procedures requirements?	<input type="checkbox"/>
	How are you going to ensure your responsibilities map is up to date?	<input type="checkbox"/>
	Have you addressed the overall responsibility requirements?	<input type="checkbox"/>
Human resources functions	Do you need to review and update your employment contracts?	<input type="checkbox"/>
	Are revisions to policies and procedures required?	<input type="checkbox"/>
	How are criminal records checks and regulatory references going to be addressed both on recruitment and ongoing?	<input type="checkbox"/>

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