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FINANCIAL SERVICES FACULTY

SENIOR MANAGERS AND CERTIFICATION REGIME

Inspiring confidence in financial services

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Senior Managers and Certification Regime
The Senior Managers and Certification Regime (“SMCR”) is a new regulatory framework which aims to improve individual accountability. First introduced in March 2016 for banks, building societies and large investment firms, the regime is being extended to solo firms.

It replaces the Approved Persons regime and arose in response to the Parliamentary Commission on Banking Standards’ investigation into the causes of the 2008 financial crisis.

The new regime seeks to allocate responsibilities to specific, named individuals, to ensure that key staff and directors can be held accountable should problems arise and take steps when needed.

Section 1
Overview

Background
The 2008 financial crisis exposed significant shortcomings in bank governance, culture and staff behaviours. The regulatory response, the Senior Managers and Certification Regime (“SMCR”), was introduced in March 2016 for dual-regulated firms. They are the firms regulated by both the Prudential Regulation Authority and the Financial Conduct Authority and includes banks, building societies and the larger investment firms. From December 2019 the regime is being extended to solo-regulated firms (e.g. consumer credit firms, financial advisers, investment managers, mortgage lenders, payment institutions and wealth managers).

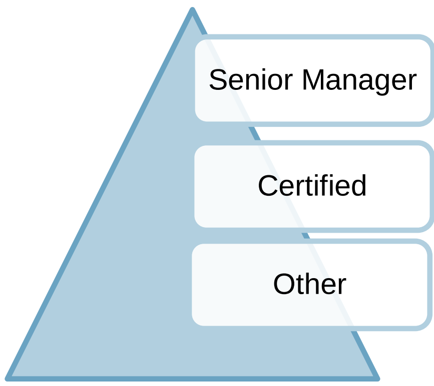
It introduces a comprehensive approach for the allocation of responsibilities to ensure that key staff and directors can be held accountable should problems arise and to ensure they are clear who should deal with smaller issues proactively. The aim is chiefly prevention - to reduce significant issues emerging by making individual accountability clearer earlier. It is not intended to be an enforcement led approach.

How the regime works
The regime has three key parts:

I. Senior managers - there are formal rules for new appointments at the most senior level and nine conduct rules apply to them.

II. Certified staff - the next layer of staff are individuals who are certified by their employer to perform 'significant harm functions' or who are 'significant risk takers'. They are subject to the five individual conduct rules.

III. Other/Code of conduct staff - the remaining staff within relevant firms are not certified. They are however, still subject to the five individual conduct rules.



Section 2

Links to regulations and references

Using the links and margin notes in this document

The notes in this Helpsheet identify relevant statements and other regulations – these sections cannot be considered in isolation when applying them in practice.

You might find it useful to download relevant section(s) of the regulation(s) so that you can refer to them when using this document.

Make sure that you use the right version of the regulations or standards

Standards and regulations are often updated and amended, and may have transitional provisions. It is important to use the right version, and to make sure that it applies to the relevant time period.

Regulations and References
Bank of England Supervisory Statement 28/15
PRA strengthening accountability webpage
FCA SMCR webpages
FCA solo regulated firm guidance
FCA guide for solo firms
FCA PS 18/14
Senior manager conduct rules
Individual conduct rules

Section 3

Key Features of SMCR

I Senior Managers
These are the most senior people in a firm performing senior management functions (“SMF”). They require regulatory approval before commencing their roles. The fitness and propriety of senior managers must be verified.

a) Fitness - can they do the job, do they have the skills etc.
b) Propriety - are they likely to act with integrity

Firms are therefore expected to have carried out appropriate due diligence on SMF candidates including assessing their suitability for the role, performing criminal record checks and obtaining references from previous employers. At least once a year, firms must also reassess whether senior managers remain suitable for their roles. An additional requirement is for outgoing SMFs to prepare a handover document for the person commencing the role.

Every SMF holder is required to have a documented **statement of responsibilities**, which sets out the areas of the business they are responsible and accountable for. SMFs will also be allocated specific “**prescribed responsibilities**” applicable to their role and specified by the regulator. SMFs have additional rules they must follow - the Senior Manager Conduct Rules.

1. Take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively.
2. Take reasonable steps to ensure that the business of the firm for which you are responsible complies with the relevant requirements and standards of the regulatory system.
3. 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.
4. Disclose appropriately any information of which the FCA or PRA would reasonably expect notice

A firm’s overall SMCR arrangements must also be documented within an up-to-date “**Responsibilities Map**”. This will record how accountability is allocated, the firm’s committee structure and the governance arrangements it applies.

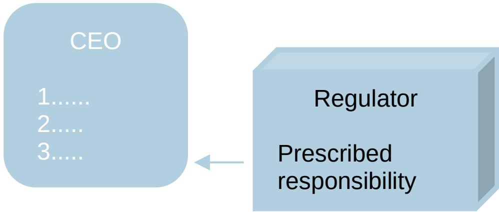
II Certification Regime
The Certification Regime applies to employees whose role may mean it is possible for them to cause 'significant harm' to the firm or its customers. For example, could someone in Sales sell an inappropriate product to a vulnerable customer or could a trader manipulate a key market price to mislead other market participants and thereby undermine the market's integrity. These roles are called 'certification functions' and these individuals must follow the five **Conduct Rules**.

Individuals performing certification functions do not require regulatory approval. However, the regulated firm must satisfy itself on an annual basis that the individual is fit and proper to be certified. This may fit in with an annual staff appraisal process.

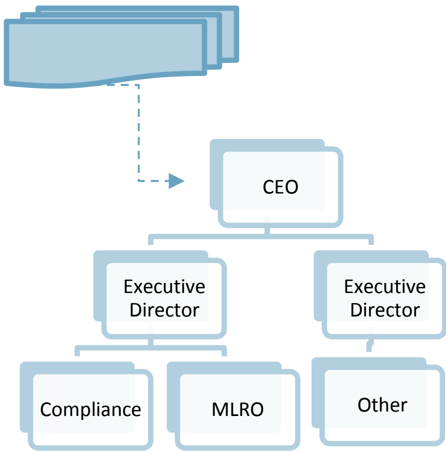
III Code of Conduct
The remaining staff within a dual-regulated firms, apart from those performing ancillary roles such as receptionists or security guards, are also subject to the **Conduct Rules** applicable to certified staff. Firms must ensure that these members of staff are provided with training on the rules and the potential impact of breaching the rules. Equally, firms are obliged to submit a regulatory notification if a breach of a conduct rule is identified within the firm.

SMCR for Solo-Regulated Firms
The FCA have published the near-final rules on the forthcoming extension of SMCR to solo-regulated firms. This means that a range of firms including investment firms, asset managers, insurance and mortgage brokers and consumer credit firms will be within the scope from 9 December 2019.

Statement of Responsibilities



Responsibilities Map



Conduct Rules

1) Act with integrity.
2) Act with due skill, care and diligence.
3) Be open and cooperative with the FCA, the PRA and other regulators.
4) Pay due regard to the interests of customers and treat them fairly.
5) Observe proper standards of market conduct.

The full application of SMCR for insurers will commence on 10 December 2018.

While the extended regime will feature many of the same requirements as SMCR for dual-regulated firms, it will be applied in a proportionate way depending on the scale and complexity of the relevant firm. To this end, the near final rules introduce three classifications of firms; namely **Enhanced**, **Core** and **Limited Scope** firms.

The Core regime will apply to the majority of FCA solo-regulated firms. The Enhanced regime will apply to an estimated 350 firms that have more complex businesses and these firms will be subject to additional requirements. Limited Scope firms (for example, limited permission consumer credit firms) will have fewer SMCR obligations than Core firms. However, the certification requirements for individuals will apply equally to each firm type under the extended regime. Firms will have to identify their certified population from the commencement of the extended regime (December 2019), but they will then have 12 months to complete fitness and propriety assessments and issue certificates.

The FCA has set out the criteria that will determine whether a firm will be defined as Enhanced. A firm will be captured if one or more of the criteria apply.

Impact of Firm Classification
Depending on the SMCR designation attributed to individual firms, different SMFs and prescribed responsibilities will apply:

- Limited Scope Firms – there are three SMFs within the Limited Scope tier. The number of functions applicable to a Limited Scope firm will also depend on specific permissions and activities. Prescribed responsibilities are not applicable to Limited Scope firms;

- Core Firms – there are six SMFs and five prescribed responsibilities applicable to Core firms;

- Enhanced Firms – there are 17 SMFs and 12 prescribed responsibilities applicable to Enhanced firms.

SMCR is applied at a legal entity level. So a large group may contain Enhanced, Core and Limited Scope firms.

	Dual (PRA & FCA)			Solo (FCA only)
	Banks	Designated investment firm	Insurer	Various
March 2016	SMCR		SIMR	APER
Dec 2018	SMCR			APER
Dec 2019	SMCR			

Enhanced firm criteria

- Significant investment (IFPRU) firms;
- CASS large firms;
- Assets under management of £50bn or more as a thee year rolling average;
- Total intermediary regulated business revenues of £35mn or more per annum, calculated as a three year rolling average;
- Regulated revenue generated by consumer credit lending of £100mn or more p.a., calculated as a three year rolling average; or
- Mortgage lenders (that are not banks) with 10,000 or more regulated mortgages outstanding.

Enhanced	Core	Limited Scope
- 12 Prescribed Responsibilities - 17 SMF roles - Certification regime - Extra rules	- 5 Prescribed Responsibilities - 6 SMF roles - Certification regime - Core rules	- 0 Prescribed Responsibilities - 3 SMF roles - Certification regime - Fewer rules
c.350 firms	Majority of solo-regulated firms	

Section 4

Key actions

Preparation and implementation

1. Use the regulators' guide and firm checkers to identify how your firm fits in the new regime; the scale and the timing of the requirements that will apply to you.

2. Identify the population of senior managers and certified staff at your firm. They should cover all major functions, operations and business lines leaving no significant area uncovered.

3. Write a 'statement of responsibilities' for each of your SMF roles (ideally a standalone document of c.300 words and not reams). These will be needed from 'Day 1' and might form part of an individual's contract. You should allocate 'prescribed responsibilities' as appropriate. If a responsibility is shared then any enforcement action may be directed at both delegates. As a SMF are you clear on the responsibilities that have been allocated to you?

COCON 4.1

Example: applying SMCR to FCA

4. Develop the firm's overall responsibilities map. This may need to reflect matrix structures, an international dimension and/or branches and subsidiaries.

5. Run a scenario session for your SMFs to understand if any more clarity is needed. How would things work in normal and crises situations?

6. Train you certification staff. Do they understand and comply with the conduct rules? Are they fit and proper?

7. Review your talent induction, performance review and reward processes. Will you have to redesign your fitness and propriety tests? How will you annually certify individuals and evidence this process?

8. Review your governance framework with the new accountability allocation in place. Is there an opportunity to reduce the number of meeting attendees (e.g. should it be just those who are accountable)? Would your governance arrangements identify significant exceptions?

9. Do you have whistleblowing processes and a 'speak-up' culture so you can evidence that you are taking 'reasonable steps' to escalating critical issues.

Ongoing

10. As an SMF, are the steps you are taking in discharging your responsibilities reasonable? Have you identified the root cause to any issues, do your controls work and can you evidence their effectiveness? What testing and assurance do you have?

11. Can you evidence that you have taken reasonable steps? Have you made a record of any aspects that concern you? Have you communicated these concerns through the appropriate channels (e.g. regulators, where appropriate)?

12. Review your management information (MI) pack. Does it allow you to make decisions quickly and robustly?

13. Do you have the right team and skilled resources to manage the key risks to your organization? Does their skill set allow you to delegate appropriately and help you to meet your obligations?

14. What are your handover arrangements as and when people leave?

15. Bring you statement of responsibilities to regulatory interviews and be prepared to answer questions around how you have delivered against your responsibilities. They will ask what you have been doing, not what your employer has done.

16. As an SMF, think about your role as a leader and driving the right culture. 'Your actions are your monuments'.

Section 5

Key Challenges

Lessons
SMCR is a relatively new regulatory framework but some challenges are being seen at those firms caught in the first wave of implementation:

1. There has been a lot of focus by some firms and individuals on evidence so that they can demonstrate that they have taken reasonable steps. It may be helpful to create a personal record initially but at some point be sure to escalate any concerns appropriately.

2. There is the risk of information overload and inflation of management information packs (MI) as junior individuals may seek to demonstrate that they have acted reasonably by escalating everything. It is the responsibility of the committee chair or line manager receiving the MI pack to challenge the appropriateness of the MI in terms of its quantity and quality.

3. Regulators have said that the purpose of the regime is to transform the culture in financial services. Their aim is to reduce harm to consumers and strengthen market integrity. The regime seeks to achieve it outcome through 'prevention' and reducing risks. It is not intended to be an enforcement led regime. So building a framework alone will not be what gets you 'out of jail'. Think about how your implementation would surface and manage issues in real life.

4. It is still ok to delegate under SMCR (SMF Rule 3) but as an SMF you must still provide oversight. This may mean some testing of the information from your direct reports: rather than a trust-based model of supervision. Should any issues emerge there is the risk the regulators will apply the 'hindsight lens' to assess whether your supervision was appropriate.

5. There is the risk that a unitary board could become anything but as individuals seek to demonstrate that they had exercised caution and can evidence through the board or committee minutes that they have exercised robust challenge. The Chair's role is to support the effectiveness of the board and to guide directors appropriately.

   PRA - Board responsibilities SS 5/16

6. Whilst the regime has brought some benefits, like fewer traders breaching their limits, there will be an additional cost for the extra HR processes (e.g. updating employment contracts, annual certification/appraisal processes and HR disciplinary procedures).

7. There are a number of areas where a firm might legitimately exercise judgments under SMCR. For example, do you choose to operate a zero tolerance policy when incidents arise or is it 'three strikes and you're out'? Similarly, how to treat individuals who have been part of incidents in the past is for you to consider in the circumstances given the risk of the role they will be undertaking and the severity on any past issues.

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Contacts and further help

Helpsheets for faculty members

This Helpsheet is part of a series designed to provide practical help for Financial Services Faculty members in exercising their professional judgement.

The Faculty cannot offer interpretations of standards or give views on the application of regulations to particular companies or transactions.

Helpsheets

Topics covered by other Helpsheets include:

- Fair & Effective Markets Review
- Assurance reports on benchmarks and indices
- Banking regulatory ratios: ICAEW assurance framework

A complete list of Helpsheets can be found here:

https://www.icaew.com/en/technical/financial-services/fs-helpsheets

Helpsheet comments and suggestions

To comment on Helpsheets, or to suggest topics that you'd like to see covered by Helpsheets, email us at fsf@icaew.com

Faculty resources

Resources published by the Financial Services Faculty may be found here:

https://www.icaew.com/en/technical/financial-services/financial-services-faculty

Resources include online access to the faculty's publications, webinar recordings and other guidance.

The Financial Services Faculty

The faculty aims to help members keep up to date with the implications of new standards, regulations and practice in financial services.

Our international community of financial services professionals also contribute to the ICAEW's work in influencing the development of financial services laws and regulations.

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