

A panoramic view of the London skyline at sunset. The sky is a mix of grey and orange, with the sun low on the horizon. Key buildings like the Shard, the Gherkin, and the London Bridge are visible. A blue banner is at the bottom.

Launch of the SM&CR and the interaction with MiFID II

29 June 2017

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PRECISE. PROVEN. PERFORMANCE.

Agenda



1. **Introduction** - Kelly Sheppard, Partner
2. **Overview of the SM&CR** - Teresa Mazur, Associate Director
3. **SM&CR: banana skins** - Andrew Jacobs, Director
4. **Governance and organisational requirements: MiFID II interaction with the SM&CR** - Giovanni Giro, Senior Manager
5. **Conclusion** - Kelly Sheppard, Partner

Introduction

Kelly Sheppard, Partner

Introduction



- Survey results
 - 54% of firms have done some high level planning in respect of the SM&CR
 - 88% of firms are not sure that they will be ready for MIFID II on 3 January 2018
- It is anticipated that some 52,000 firms will come under the new SM&CR and some 92,000 individuals will now need to be registered.

Overview of SM&CR

Teresa Mazur, Associate Director

Why SM&CR was introduced



- SM&CR is an accountability framework. It was put in place following a review by the Parliamentary Commission on Banking Standards (PCBS), on professional standards and culture in the UK banking sector
- Improving standards within relevant firms is important to restore trust in financial services
- The existing Approved Persons regime operates purely as a gateway
- SM&CR does not change firms' corporate responsibility

Why individual accountability matters



- Clarity for firms and regulators about each senior manager's responsibilities
- Important part of the regulators' drive to raise standards of individual conduct across the financial services industry
- Linked to the FCA's Business Plan 2017/18 priority 'Firms' culture and governance':

Outcomes we seek...

Firms develop a culture of accountability at all levels and senior individuals are fully responsible and accountable for clearly defined business activities and material risks...

- Senior managers need to ensure that their firm's business processes, people and other drivers of culture support and reinforce a culture that works in the long-term interests of the firm, its customers and market integrity

Extending the regime: who, when & how

Which firms are affected



Current regimes

- SM&CR applies to UK banks, UK branches of foreign banks, building societies, credit unions and PRA designated investment firms
- Fewer of the Senior Managers Regime requirements apply to firms with gross total assets of £250m or less
- Senior Insurance Managers Regime applies to (re)insurers

•Extending the regime

- The SM&CR will be extended to apply to all financial services that fall under FSMA
- The intention is for the extended regime to become effective in 2018

Which individuals are affected



Element of SM&CR	Impacted staff and directors
Senior Managers Regime	<ul style="list-style-type: none">• Performs key role, eg, CEO, CFO, Chairman• Holds key function – has overall responsibility for a whole area of the firm• Including NEDs excluding Notified NEDs
Certification Regime	<ul style="list-style-type: none">• Material Risk Taker / Significant Harm Function• Previous Significant Influence Function• CF30 with a qualification• Line manager of Certified Person
Conduct Rules	<ul style="list-style-type: none">• All employees and directors other than ancillary staff

How and when?



- The PRA and FCA are consulting on how SM&CR will be adapted and applied to the diverse range of regulated firms
- Proportionate application of SM&CR to reflect the size and complexity of firms

The Bank of England and Financial Services Act 2016 extends the SMCR to all sectors of the financial services industry. It also allows us to apply all elements of the regime to insurers. We intend that our extended regime will be clear, simple and proportionate. During Q2 of this year we will be consulting widely with industry, firms and consumers on our proposals. We expect implementation to begin from 2018.

SMCR: One year on – FCA news – March 2017

Key elements of the current regimes

Key elements of SM&CR



Senior Managers Regime

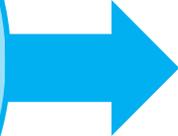
- Identify and allocate Senior Management Functions (SMF) to named individuals
- Lighter touch for small firms
- ‘Statement of responsibilities’ (SoR) setting out each Senior Manager’s specific responsibilities
- ‘Responsibilities map’ describing management and governance arrangements in comprehensive detail, including non-UK and non-regulated activities

Key elements of SM&CR



Senior Managers Regime

Duty of responsibility



- Senior Managers required to take 'reasonable steps' to prevent regulatory breaches in their areas of responsibility
- Burden of proof lies with the regulators
- Outgoing Senior Manager to take reasonable steps to ensure an orderly handover

Key elements of SM&CR



Certification Regime

- Certify as 'fit and proper' any individual who performs a function that could cause 'significant harm' to the firm or its customers
- Ongoing firm assessment of fitness and propriety – at recruitment stage and annually
- Reassess if function changes
- Regime allows for up to four weeks' cover where the role does not require qualifications

Key elements of SM&CR



Certification Regime

'Fit and proper' assessment

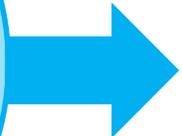
- Personal characteristics (including good repute and integrity)
- Competence, knowledge and experience
- Relevant qualifications
- Appropriate training
- Due diligence evidence to include:
 - past business conduct references/ regulatory references
 - criminal records checks

Key elements of SM&CR



Conduct Rules

First tier – applies to all employees (excl. ancillary support staff)



Individual Conduct Standards

- You must act with integrity
- You must act with due skill, care and diligence
- You must be open and cooperative with the regulators

Additional FCA Conduct Rules

- Pay due regard to the interests of customers and treat them fairly
- Observe proper standards of market conduct

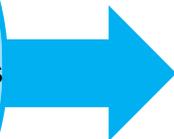
Consistent with current Statements of Principle for Approved Persons

Key elements of SM&CR



Conduct Rules

Second tier – Senior Manager rules



- You must take reasonable steps to ensure that the business of the firm for which you are responsible is **controlled effectively**
- You must 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
- 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
- You must **disclose appropriately** any information of which the FCA or the PRA would reasonably expect to have notice

How the extended regime will affect your firm

How the extended SM&CR might look



- The framework of the regime will be the same as the existing SM&CR – the detail will be subject to consultation due later this year
- The duty of responsibility will apply to all firms (as per the FCA's Policy Statement PS17/9)
- SMF holders will still require regulatory approval
- Anticipated that Notified NEDs will not need SMF approval
- Anticipated that current customer facing CF30 approved persons will no longer require SMF approval. May need to be certified
- Grandfathering over of current Approved Persons is likely, given how the existing regime was implemented

How the extended SM&CR might look like



- Implementation of the SMCR might be phased, as it was for banks
- Anticipated that small firms will be subject to fewer of the SM&CR requirements or at least a watered down version – uncertain what this will look like in practice
- Regulatory references will probably be required for Senior Managers and certified staff
- Firms will almost certainly be required to train staff on the Conduct Rules
- We will probably see more disciplinary action by regulators against individuals who are Senior Managers

How firms can prepare for the extended regime

To start now...



- Categorise staff
- Allocate individual responsibilities
- Statements of responsibilities
- Responsibilities map (smaller, less complex firms will have simpler maps)

Responsibilities map includes:



HR, Compliance & Legal need to be involved from the outset

Plan for other tasks...



- **'Fit and proper' assessments**
- **Staff training:**
 - Conduct Rules – virtually all staff
 - Maintaining fitness & propriety of staff who will fall under the Certification Regime
- **Contractual considerations:**
 - Employment contracts
 - Staff handbook, internal codes of ethics/conduct
- **Breach reporting**
- **Leavers:**
 - Provision of regulatory references
 - Handover procedures for senior managers
- **Ensure adequate resourcing** – HR, Compliance and Legal (particularly HR who will have ongoing increased workload)

Conclusion – Be prepared!



- **Forewarned is forearmed:**
 - We know the extension of SM&CR is coming
 - We know that, as a minimum, the basics of the current regime for banks will apply across all firms
 - SM&CR extension will mean significant change for most affected firms – implementation and on-going compliance
 - Get your project team together – include HR, Compliance and Legal
 - Plan your work-streams and timescales
 - Ensure adequate resourcing for implementation and the future – especially HR

Start now - don't wait until the FCA consultation has been completed!

SM&CR: banana skins

Andrew Jacobs, Director

SM&CR: composition



- Practical experiences
- Findings documented in FS 16/6, 16/7 & 16/8
- Learnings from our clients
- Best practises from peers and regulators

- “..the Senior Managers regime is firm wide issue for firms”

Andrew Bailey, June 2016

The common banana skins



1. **Detail:** insufficient detail to delineate the scope of an individual's responsibilities, the specifics of responsibility
2. **Lack of clarity:** Responsibility Maps unclear about who is the most senior person with responsibility and confused about non-executive oversight
3. **Incompleteness:** aspects of responsibility sharing are not adequately addressed
4. **Lack of transparency:** group considerations
5. **Dynamic in nature:** firm's arrangements not reviewed and updated regularly or ongoing certification and notification requirements were overlooked

Examples of where detail has been missed



Confusion re. Notified Non Executives

Confusion re. Non-Executive Oversight

Inconsistencies between documentation

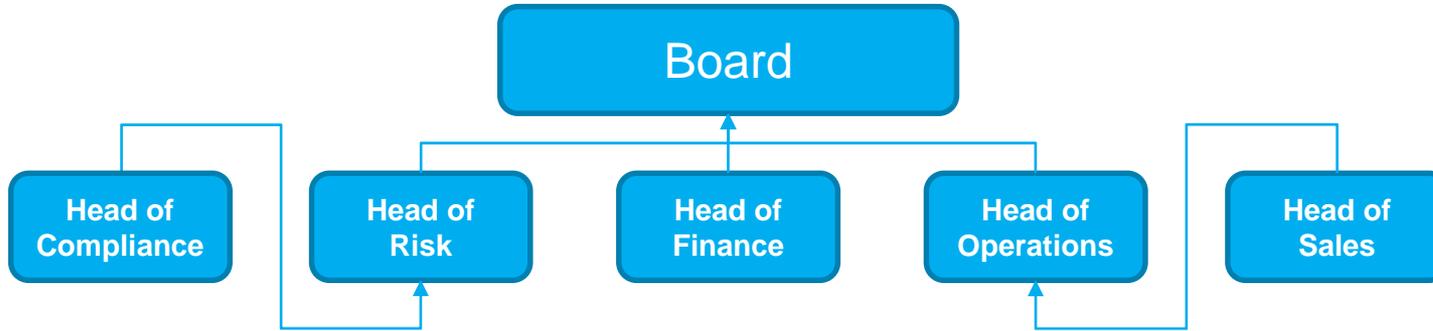
Not identifying all business activities

Failure to meet 'practical and useable' guidelines - SYSC 10C.11.25G

Overreliance on SYSC 4 Annex 1G

Issues with job titles

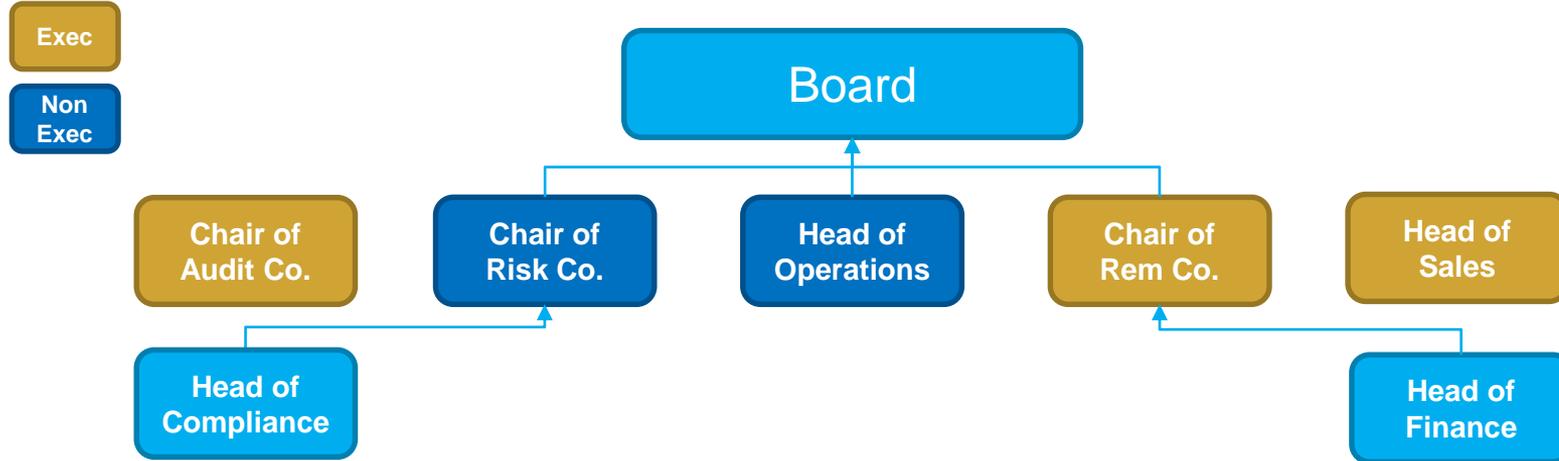
1) ExCo example



SYSC 4.7 (5-8R & 13G):

- Requirement to allocate prescribed senior management responsibilities to one or more senior managers of the firm and must make clear the allocation of the above, in such a way that it is clear who has which of those responsibilities
- At all times, one or more of its SMF managers must have overall responsibility for each of the activities, business areas and management functions of the firm

2) Board example



SYSC 4.7/11

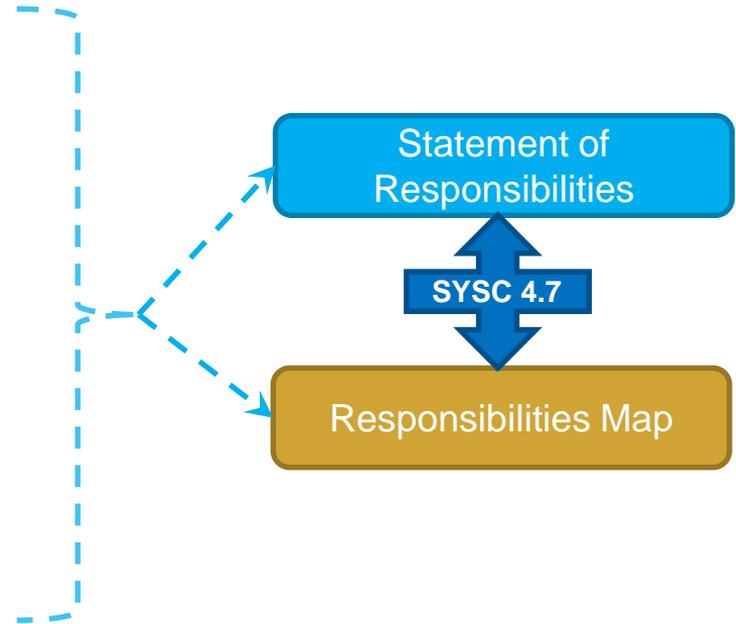
- a person having overall responsibility for a function means a person who has ultimate responsibility (under the governing body) for managing or supervising that function and primary and direct responsibility for briefing and reporting to the governing body about that function and putting matters for decision about that function to the governing body

3) Responsibility sharing



Firms should challenge themselves about:

1. Clarity, detail, overlaps and gaps
2. Whether individuals actually understand the extent and limitations of their shared responsibility
3. Is the sharing of responsibilities necessary and justified?
4. Guidance in SUP in respect of sharing and dividing responsibilities when drafting a SoR.
5. In instances where an individual shares a certification function, each individual performing that function will need to be assessed. Conversely, where an individual performs multiple certification functions their fitness and propriety for each function will need to be assessed



Group considerations



Responsibility Maps: Group considerations, management responsibilities and governance

- Must include details of how the firm's management and governance arrangements fit together; detail the extent to which the firm's management and governance arrangements are provided by, or shared with any other members of its group or others

- A lack of clarity on how the relationship between the firm and group influences or impacts the firm and the senior management responsibilities in practice

Clarity in respect
of group
interaction

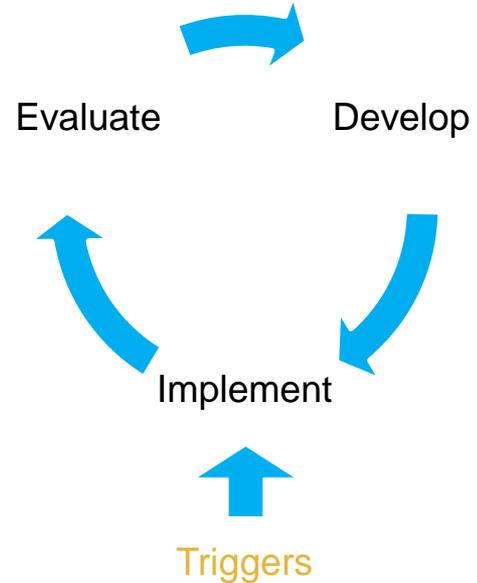
- A 'Group Entity Senior Manager' will be introduced to bring individuals employed by a parent, holding or other group undertaking that exercises significant influence into scope of the regime

- Where a firm reports to a group function that has a strong influence on the decision making process within the firm, these functions will usually be subject to the SMR

Ongoing considerations



- Initial requirements
- Ongoing requirements
- Exit requirements:
 - Senior Managers Regime
 - Certification Regime / Conduct Rules
- Duty of responsibility:
 - What constitutes reasonable?
 - How to demonstrate the steps taken?
 - How you should respond if something goes wrong?



SM&CR: Common Misconceptions



SM&CR is owned by Compliance

No involvement is needed from other business areas

Minimal crossover and linkage with other systems/process

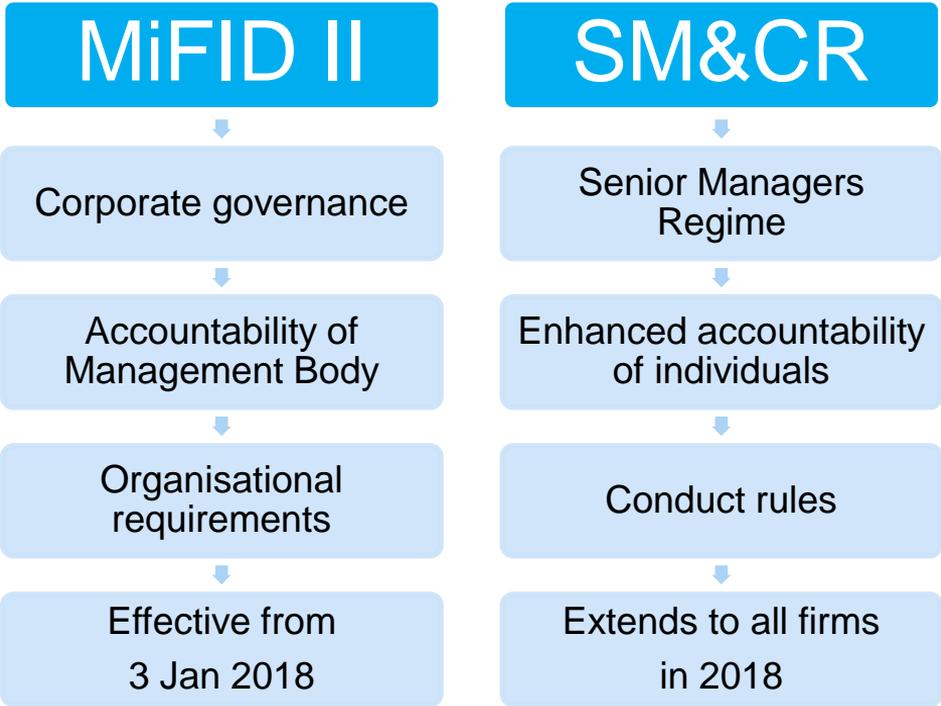
SM&CR does not involve any sensitivities

SM&CR is simply an iteration of the Approved Person's regime

Governance and organisational requirements: MiFID II interaction with the SM&CR

Giovanni Giro, Senior Manager

MiFID II and SM&CR



Management Body



- New definition of Management Body with extended responsibilities around governance (art. 9 MiFID II):
 - Overall strategy
 - Governance arrangements and segregation of duties
 - Organisation of the firm's business
 - Access to management information
 - Oversight of skills and competence of personnel
 - Conflicts of interest policy
 - Remuneration policy
- Extended application of CRD IV standards to all common platform firms

Members of Management Body



- Individual Members of the Management Body are personally accountable for:
 - Sufficient time allocation
 - Limited number of other directorships
 - Good reputation, skills and competence
 - Decisions subject to challenge and scrutiny
 - Subject to FCA assessment
- At least two executive members in Management Body
- Chairman ≠ CEO
- 1 executive directorship + 3 non-executive directorships

Organisational requirements



- New organisational requirements (art. 16 MiFID II):
 - Effective governance arrangements
 - Documented decision-making procedures
 - Clear organisational structure and reporting lines
 - Risk management framework
 - Products and services governance policy and stress testing
 - Initial and regular competence reviews
 - Induction and training
- Management Body supported by Senior Management and independent Compliance and Risk functions

Analogies and overlap with SM&CR



MiFID II

SM&CR

Management Body role and function



Requirements for Senior Managers

Criteria for selection of members of Management Body



Enhanced competence and fit and proper standards

Allocation of responsibilities and segregation of duties



Statement of Responsibilities of SMF and Certified Person

Corporate governance structure and arrangements



Responsibilities map and Certification policy

Key considerations



Review Board composition and selection criteria

Update corporate governance policy

Coordinate MiFID II and SM&CR requirements

Assess skills and competence of all staff

Review individual roles and reporting lines

Management Body \neq SMF

Training