

## SENIOR MANAGERS AND CERTIFICATION REGIME

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Summary of PS 18/14 – Extending the Senior Managers & Certification Regime to FCA firms - Feedback to CP17/25 and CP17/40, and near-final rules  
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# Introduction

## Document Purpose

The Financial Conduct Authority (**FCA**) has provided feedback and near final rules following its consultation paper in July 2017 titled '*Individual Accountability: Extending the Senior Managers & Certification Regime to all FCA firms*' and its December 2017 consultation paper dealing with transitional arrangements from the Approved Persons Regime (**APER**) to the Senior Managers and Certification Regime (**SM&CR**). The rules may however be amended with subsequent handbook changes, for example those relating to the UK's exit from the European Union.

This note has been prepared with a view to focusing on the key areas of change following the previous consultation's papers and assumes some knowledge of the proposed regime. We have also included some helpful areas of clarification provided by the regulator.

## SM&CR Overview

SM&CR will be extended to insurers on 10th December 2018 and to all other firms on 9th December 2019. The near final rules for extension to insurers and other firms were published on 4th July 2018, together with a consultation paper on a financial register for all approved senior managers and certified staff covering all firms.

The aim of SM&CR is to increase accountability of individuals and to influence the behaviours of individuals and ultimately culture in the financial services sector.

The extended regime has been adopted to enable a proportionate approach; dependent on the size complexity and sector of the firm. This note focuses on SM&CR rules for non-insurers who will be covered by the regime on 9 December 2019. This note should be read in conjunction with our note on the financial register consultation called "Introducing the Directory".

The new regime consists of three core components: the Senior Managers Regime, the Certification Regime and the Conduct Rules. Rules are then applied in a proportionate way depending on the tier in which the firm sits, these tiers are summarised below:

- ▶ Core firms subject to a baseline of SM&CR requirements, which will apply to the majority of firms.
- ▶ Limited scope firms will mainly be focused on Limited Permissions firms within the consumer credit sector.
- ▶ Enhanced firms (i.e. larger firms) will be subject to additional requirements. The FCA has adjusted the qualifying criteria. the changes are for firms with:
  - Current total regulated intermediary business revenue of £35m or more per annum, calculated as three year rolling average
  - Annual revenue generated by regulated consumer credit lending of £100m or more, calculated as a three year rolling average
  - Non-bank mortgage lenders and administrators with 10,000 or more regulated mortgage contracts outstanding

Senior Managers will have a "duty of responsibility". This means that FCA can take action against a senior manager where any breaches or contraventions occur in their area of responsibility, if the FCA can demonstrate that the senior manager did not take reasonable steps to prevent the breach occurring or from continuing.

SM&CR largely replaces the previous APER regime. It is based around senior management functions (**SMFs**) being allocated to senior managers who have documented "Statements of Responsibility" that detail the senior manager's areas of responsibilities and accountabilities. These individuals must be approved by the FCA before carrying out the relevant SMF(s). Enhanced firms must go further and allocate "overall responsibility" to one or more senior managers (with no gaps) for every business unit, activity or area of the firm that relates to regulated activities or is a activity which is related to regulated activity or is an activity that is held out to be for the purposes of a regulated activity. This involves mapping out all the different business units, activities and areas of the firm, including both front office and back office functions in a single documents referred to as a responsibility map.

Employees who could cause significant harm to the firm, the market or customers (which are not SMFs) must be annually certified (**Certified Persons**) by the firm as fit and proper to carry out that role.

New "Conduct Rules" will replace statements of principle and the code of practice under the Approved Persons Regime. Conduct Rules will apply to all individuals within the firm (involved in activities relating to the firm's regulated business and certain unregulated activities) except for employees involved in the provision of ancillary services only (e.g. receptionists, post room staff).

## Key changes from the previous Consultation Papers

KEY CHANGES	EXPLANATION	FCA HANDBOOK REFERENCES
<b>Removal of the Prescribed Responsibility (that only applied to Core firms) to inform the governing body of their legal and regulatory obligations</b>	<p>In CP17/25, the FCA proposed a prescribed responsibility for ensuring that the governing body is informed of its legal and regulatory obligations has been removed on the basis that the FCA does not think it is appropriate to allocate this to one senior manager.</p> <p>Further, the FCA is of the view that under the Conduct Rules, senior managers must already ensure that the business area for which they are accountable complies with the relevant requirements and is controlled effectively.</p>	24.2.6R - Table of Prescribed Responsibilities
<b>Provide an easy process for firms to tell us they wish to voluntarily apply a higher regime tier</b>	<p>The FCA restated that SM&amp;CR applies to legal entities rather than to groups. One of the unintended consequences of the regime is that different regulated entities within groups could end up sitting within different SM&amp;CR tiers which would prevent groups from applying a consistent approach to the regime.</p> <p>Originally the FCA had indicated in CP17/25 that in order for a 'limited scope' or 'core' firm to voluntarily upgrade its tier from to 'enhanced', it would need to secure this change by way of having a requirement placed on the firm by the FCA. This would have the unintended consequence of being displayed on the FCA's public register with reputational consequences prompting a question as to why that action had been taken by the regulator.</p> <p>Firms (particularly those within groups) are now being given the opportunity to 'Opt-Up' into the enhanced tier if they wish to by making a notification with a Form O. This however would mean they are subject to all of the additional rules that an enhanced firm is subject to within 3 months of the notification being made.</p>	<p>SYSC 23 Annex 1.</p> <p>Opting-Up specifically dealt with in SYSC 23 Annex 1, 2.4G and 2.5R</p>
<b>Amend three of the Enhanced criteria to smooth single-year anomalies</b>	<p>The FCA has decided not to change the absolute level of the thresholds being applied to firms in their respective enhanced sectors. The FCA has however amended the way in which the calculation is applied.</p> <ul style="list-style-type: none"> <li>▶ Asset managers will now only be categorised as enhanced firms if they have assets under management of £50 billion or more but calculated as a three year rolling average.</li> <li>▶ Intermediaries with total intermediary regulated business revenue of £35 million or more per annum but calculated as a three year rolling average.</li> </ul>	SYSC 23 Annex 1. Table provided at 2.11G with accompanying definitions.

- ▶ Consumer credit firms with annual revenue generated by regulated consumer credit lending of £100 million or more calculated but calculated as a three year rolling average.
- ▶ Non-bank mortgage lenders and mortgage administrators with 100,000 or more regulated mortgages outstanding.

*\* no changes made to definitions of significant IFPRU firms or CASS Large firms.*

**Lengthen the time period from 6 to 12 months for a firm to implement the Enhanced tier, once they have met relevant criteria**

The FCA has increased the period of time that is permitted for firms to transition to the enhanced tier should they exceed the thresholds applied above.

This has the effect that firms moving into the enhanced tier, will have 12 months to prepare and make relevant changes so that they can comply with the enhanced requirements. As stated above, firms choosing to opt-up will only be provided with 3 months to start complying with enhanced requirements.

SYSC 23 Annex 1. Particularly sections 9 and 10.

The FCA has maintained its position that once a firm ceases to meet the above thresholds it will remain enhanced for a further 12 months.

## Helpful areas of FCA clarification

**Required Functions** – The FCA acknowledged that there may have been some confusion caused by the term 'Required Function' on the basis that some firms are not required to apply some Required Functions such as the Compliance Oversight Function. The FCA clarified that the rules have been drafted, so that if a firm does not need to have a Compliance Oversight or MLRO function under APER, then it will not need these under SM&CR.

**Legal Function** – CP17/25 highlighted that the Overall Responsibility requirement currently includes the legal function (i.e. there is no specific exemption for this function). This policy is under review following industry feedback and the position will be clarified by a further consultation before the rules come into force. No indication of the FCA's position on this was provided. However, the FCA indicated that, as the position is unclear, if a firm decided not to appoint a head of legal to be a SMF holder then it would not take action.

**Certified Persons** – The term 'Significant Harm Function' comes from Financial Services and Markets Act 2000 (FSMA). It describes a person performing these functions as someone *'involved in one or more aspects of the firm's affairs, so far as relating to a regulated activity, and those aspects involve, or might involve, a risk of significant harm to the firm or any of its customers'*. The updated FCA handbook has changed the term to 'FCA Certification Function'. The FCA confirmed that its FCA Certification Function applies only to individuals performing a regulated activity. Another point clarified by the FCA was that if an individual performs a SMF and a FCA Certification Function, then they will be subject to both senior manager and certification regimes. This means that an individual will need to have an annual certificate issued regarding significant harm functions.

**Fit and Proper** – The FCA emphasised that Fit and Proper requirements were designed to reinforce that firms need to take responsibility for their staff having the knowledge and skills to do their jobs. They also highlighted the obligation to assess fitness and propriety of senior managers and certified persons at least annually is a requirement under FSMA.

**Criminal Offences** – The FCA reaffirmed that there is no requirement for annual criminal record checks. However, the FCA expects firms to screen each senior manager for criminal record information before an application is submitted to the FCA. Conviction for a criminal offence will not automatically mean that someone is not fit and proper as per existing FIT guidance.

**Regulatory References** – The FCA reminded firms that they should already not be entering into non-disclosure agreements that could affect their ability to disclose the information required by regulatory references, or to the regulator, as such the position after SM&CR will remain the same. The FCA acknowledges that there may be situations where a candidate has not told their current employer that they are leaving their role, so it accepts that firm may not have obtained a regulatory reference before and offer and acceptance of the role. However it reminds firms, that fit and proper assessment cannot be confirmed until its due diligence is complete, which includes getting a reference from the candidate's previous employer. The FCA has considered GDPR implications of regulatory references and does not think they contravene any aspect of GDPR.

**Conduct Rules** – The conduct rules generally cover the firms' regulated activities or activities carried on in connection with a regulated activity. Furthermore, unregulated activities are covered if an issue could affect:

- ▶ The integrity of the UK Financial Services.
- ▶ The firm's ability to meet threshold conditions.
- ▶ The ability of a firm to meet requirements related to sufficient financial resources.

The regulator has clarified that the notification requirements for SMFs (which are wider than conduct rule breaches) remains at seven days but for notifications in relation to Conduct Rules breaches. The seven day time limit starts once the disciplinary action has been concluded.

For all other staff covered by Conduct Rules, these breaches only need to be notified to the FCA annually within two months from the end of 31 August, covering data from 1 September to 31 August. The only exception is Limited Permission firms whose reporting will be aligned to the existing annual reporting cycle. The FCA also clarifies that reporting requirements in respect to Conduct Rules, does not change or remove a firm's obligation to report concerns about an individual's conduct under existing rules or principles such as Principle 11.

**Forms and Connect** – The relevant SM&CR forms will be made available on the Connect system three months before the regime starts.

**Statement of Responsibility** - Whilst core and limited scope firms do not have to submit Statements of Responsibility to the regulator in advance of the 'go live' date, they do have to create and maintain them for each senior manager at the firm from the commencement of the SM&CR. Also they will need to submit Statements of Responsibility when submitting a new application for a SMF or when there has been significant change to a senior manager's responsibilities.

**Limited Permission Firm and number of SMFs** - The FCA has clarified that if a limited permission firm is required to have an MLRO and/or compliance oversight function, under another part of the handbook, then they will need to appoint SMFs for these functions.

**Certification start date** - The FCA has confirmed that the Certification regime will apply from December 2019 but firms will have 12 months to complete fitness and propriety assessments and issue certification.

## What should firms be thinking about now?

- ▶ Undertake gap analysis of existing SM&CR plans against near final rules and the Directory consultation paper.
- ▶ Identify all areas, policies and processes as well as individuals who are likely to be impacted.
- ▶ Ensure training and briefing sessions are organised for senior managers and business areas that will be impacted by SM&CR.
- ▶ Ensure you have robust plan in place to introduce day 1 (i.e. preparation for SMCR transition) and day 2 (i.e. ongoing requirements and systems required on a business as per usual basis) changes, including resources who will manage the project.
- ▶ Ensure reporting or governance arrangements for implementing SM&CR are put in place.

## Further information

Extending the Senior Managers & Certification Regime to FCA firms – Feedback to CP17/25 and CP17/40, and near final rules, [PS18/14](#), 4 July 2018

[AG FS Update](#): "Senior Managers Regime - Personal Accountability in Financial Services Firms", 22 May 2018

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