How we can help

Grant Thornton has assisted and advised a number of organisations through the implementation of the first phase of SM&CR and we are now advising financial services clients of all types in the second phase of implementation ready for 2018.

Many firms continue to believe that the implementation of SM&CR should be straightforward, however this changes the way financial services companies operate. Our experience has highlighted that many have and will struggle in areas such as:

- **Organisational structures and responsibility mapping**
- **Governance forums**
- **Offshore implications**
- **Infrastructure** (policies, procedures and mandatory form arrangements)
- **Employee awareness**
- **Training** (SM&CR and conduct)
- **Project Management and Business Analysis**
- **Embedding understanding and cultural change**

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Senior Managers and Certification Regime

Preparing for your transition
to the new regulatory regime

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Following the financial crisis, the behaviour and culture within banks came under scrutiny from regulators. This was compounded by revelations of severe misconduct or reckless risk taking by discrete groups and individuals within the industry. Part of the regulatory response to this was the Senior Managers and Certification Regime (SM&CR) which came into effect for banks and insurance companies on 7 March 2016. For senior management at these organisations, the new regime marked a significant step up in individual accountability and in the potential for long-term repercussions from behaviour or decision making which did not meet the regulator's standards.

No sooner had the regime gone live for banks and insurers, Parliament passed the Bank of England and Financial Services Act 2016 which required the Financial Conduct Authority (FCA) to extend the SM&CR to all regulated firms. This will therefore replace the current Approved Persons Regime for over 55,000 regulated firms, all of whom will be required to implement SM&CR.

Principles of SM&CR

The FCA are due to issue a consultation on SM&CR during Q2 2017 detailing how the rules which were introduced for banks and insurers will apply to regulated firms in all other sectors of the financial services industry. It will also need to address how (and exactly when) the senior managers of the 55,000 impacted firms are going to pass through the re-approval process which comes with the replacement of the Approved Persons Regime. Whilst there may be some changes compared to the banking model of SM&CR, the key principles are expected to remain the same.

Senior Management Functions

Under SM&CR, a set of Senior Management Functions (SMFs) will replace the existing Significant Influence Functions. Focusing on the most senior individuals within a firm, the SMFs must be individually identified, together with their specific role responsibilities (Statements of Responsibilities), with more precision than is typical under the Approved Persons Regime. Whilst there will be scope to 'grandfather' existing approved persons into SMF roles, SM&CR introduces new categories of Senior Manager and also requires Firm Responsibility Maps to be produced, identifying how key accountabilities have been apportioned and avoiding the sharing out of these accountabilities in a way which detracts from individual responsibility.

Certification Regime

Regulated firms will need to self-identify individuals in their ranks who are not SMFs but who could inflict significant harm on a firm, its customers or on markets. This is likely to include all individuals who face off with a customer or with a market, as well as some staff in internal facing roles. Whilst Certification staff will not need to be approved by the FCA, the regulated firm will need to have a process for assessing the behaviour of these staff, with the firm certifying their

Timeline

7 March 2016

New regime commences for banks and insurers

Conduct rule applies to SMFs

4 May 2016

Bank of England and Financial Services Act passed requiring SM&CR regime to be implemented by all regulated firms

March 2017

Conduct rules apply to all certifications of banks and insurers behaviour formally each year. Firms are also obligated to notify the FCA of any behaviour by these staff which falls below the expected standards as soon as they are aware of, or suspect, it taking place. The standards required are defined by Conduct rules and Fitness and Propriety rules.

Conduct Rules

Both SMFs and Certification staff will be expected to act with integrity, due skill, care and diligence, as well as being open and co-operative with the FCA. They will also have to act in a manner that pays due regard to the interests of customers (by treating them fairly) and observe proper standards of market conduct. Indeed these conduct rules have been made applicable beyond SMFs and Certification staff and will apply to all staff unless they fall into what the regulator defines as 'ancillary' activities, essentially low level administrative tasks. The FCA can take action against any individual that fails to meet these conduct rules, as well as regulated firms that fail to train their staff in how to meet them. Individuals who have fallen short of conduct rules must also have that evaluation included in any job reference provided on them.

SMFs also face an additional layer of conduct rules. They are required to take reasonable steps to ensure the activity they are responsible for is controlled effectively, that it complies with regulatory requirements and standards and that reasonable steps are taken to ensure any delegation of responsibilities is to an appropriate person and their work is appropriately overseen. Finally there is a requirement on SMFs to notify the FCA of any matter which the regulator would reasonably expect to hear.

Controversially the banking version of SM&CR created a criminal offence for SMFs that are responsible for a decision that causes their firm to fail. Some version of this offence is highly likely to be included in SM&CR for other regulated firms, at least for certain types of institution. More generally, the power to fine individuals through enforcement action and ban them from working in the industry will continue as before, however the application of these powers is expect to be far easier with the improved clarity over what managers are responsible for.

Fitness and Propriety

Under the new regime, firms will also be required to ensure that the identified SMFs and Certified personnel are fit and proper to perform their roles. For SMFs, this will be part of the evidence supplied to the regulator on application for role approval. Thereafter the fit and proper requirements are an annual process for firms to ensure SMFs and Certified individuals can continue in their roles. The specific fit and proper expectations are likely to be consistent with those already contained in the FCA's FIT Handbook

What can firms do to prepare

Even before the FCA consultation on the rules, there are three important steps firms should be taking immediately:

- Inform the senior individuals and any non-executive directors – briefings on the regime, taking the bank and insurance rules as the starting point to get the organisation ready, including the personal and legal implications of those roles
- Mobilise an implementation project – determining who will be accountable for leading the implementation, assigning budget and resource and identifying key stakeholders who should form part of the project's governance. This will allow the project to efficiently mobilise once the consultation is published
- Perform a high level impact assessment – using the banking and insurance roles as an indicator of the FCA's intentions, review how close the firm's current operational and governance models are to what will be required, in particular the clarity of senior accountability and decision making. This will also allow an initial view of who will be captured as an SMF, so firms can consider the desired result.

Q2 2017
FCA to consult on application and timing of SM&CR rules to all regulated firms

Q4 2017
Final rules expected for SM&CR application to all firms, including transitional arrangement

Jan 2018
Grandfathering application and live implementation