



THE EXTENSION OF THE SENIOR MANAGERS AND
CERTIFICATION REGIME (SMCR)

AN OVERVIEW

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Introduction

The Financial Conduct Authority (FCA) has published proposed rules to extend the Senior Managers and Certification Regime (SMCR) to all financial services firms.

The current SMCR model for banking firms will be applied to “enhanced SMCR firms,” (for example, asset managers with assets under management of at least £50 billion). Other firms will be subject to a lighter, less prescriptive regime.

The extension of SMCR also extends the “certification regime” under which individual firms and their senior managers (rather than the FCA) will be responsible for assessing and certifying the fitness and propriety of individuals carrying out a “certification” function on an ongoing basis.

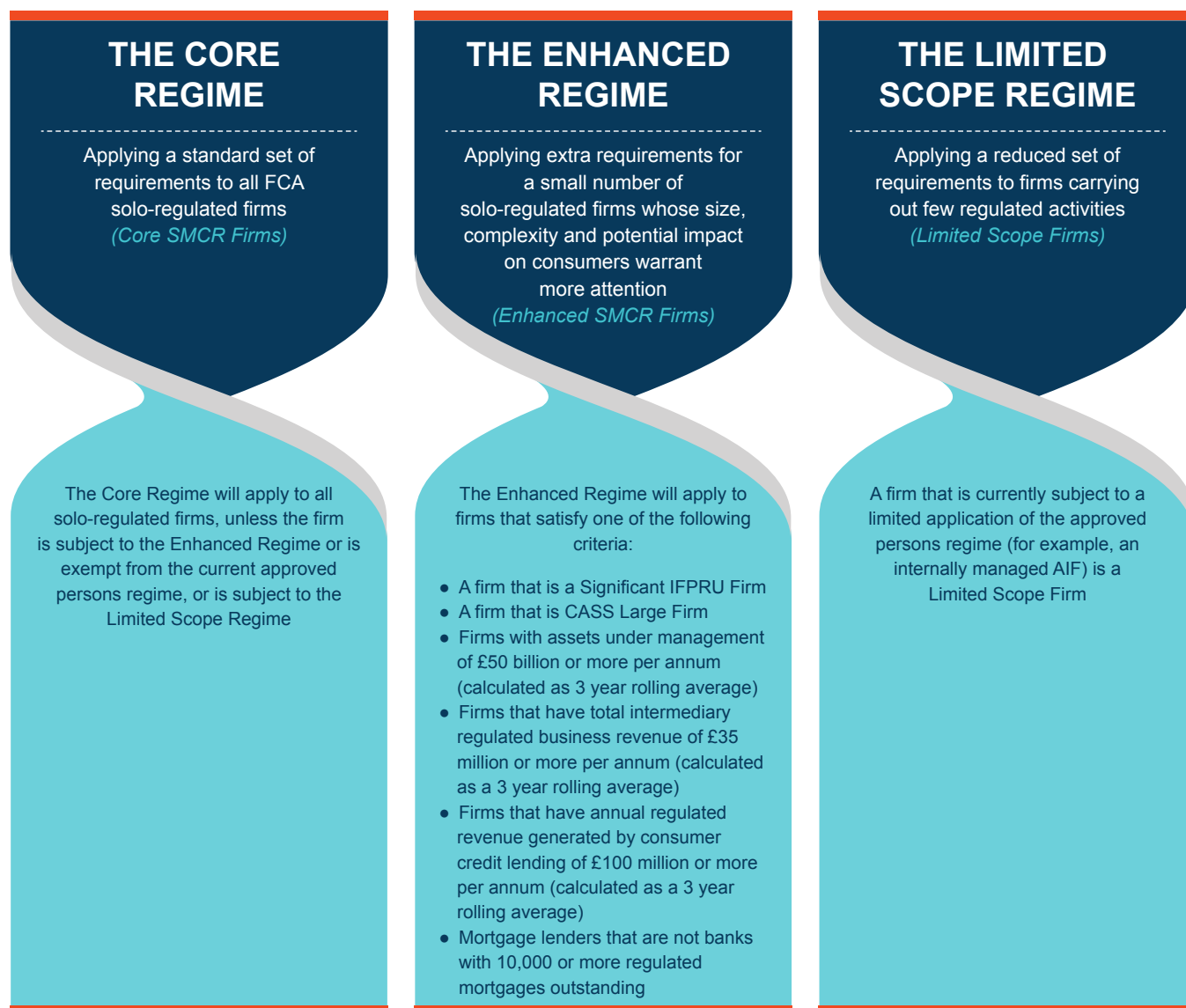
This is proposed to cover individuals presently registered under the approved person customer function as well as several other categories, including anyone who may be a material risk taker for the purposes of the FCA Remuneration Code.

New conduct rules, based on those which are currently applicable to banking firms, will apply to all firms and all of their staff except ancillary staff who do not perform a financial services role (such as receptionists, cleaners, HR administrators).

These rules will be directly enforceable and firms will be required to ensure that staff are trained in how the rules apply to them.

The rules are now final and will come into force for solo-regulated firms on 9 December 2019.

The scope of SMCR



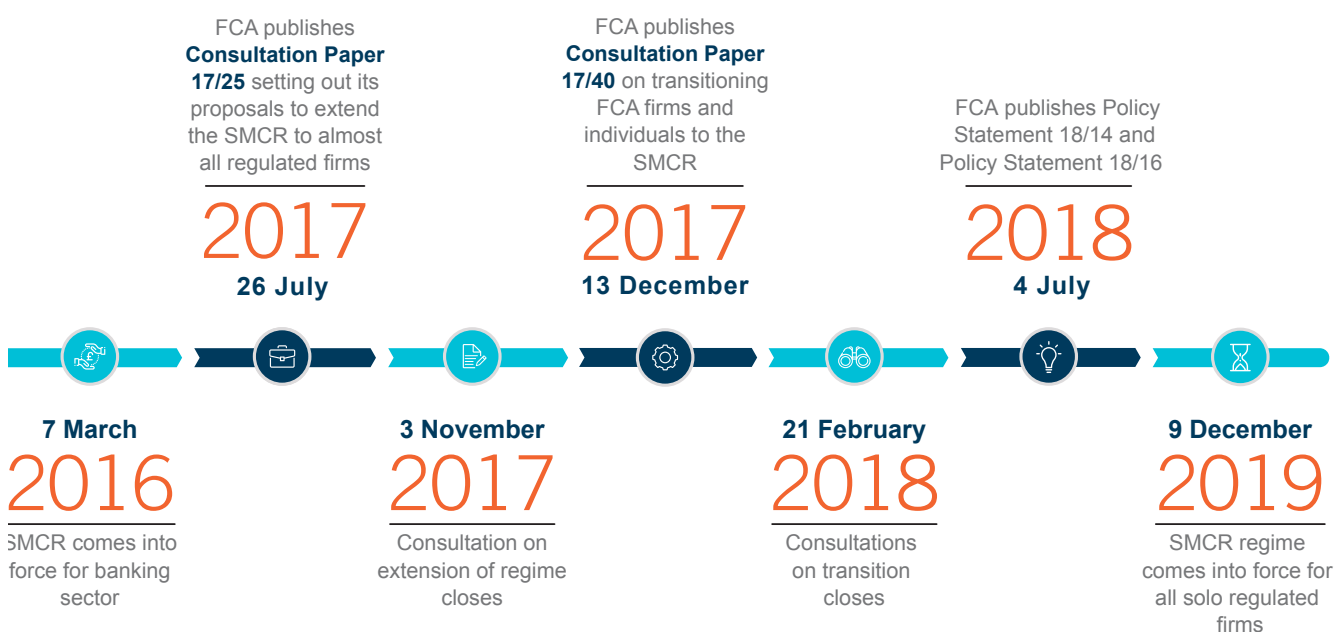
The FCA has proposed three regimes:

How can firms ensure they are prepared?

The extension of SMCR will have a significant impact on firms and there are a number of steps which firms will need to take in readiness for its introduction. Among these, firms should:

- Assess which regime applies to them: Core, Enhanced or Limited Scope.
- Identify which individuals will be performing a Senior Management Function.
- Assess each individual to ensure they are fit and proper and ensure they understand their responsibilities.
- Allocate the prescribed responsibilities (if appropriate) among these Senior Managers.
- Prepare a statement of responsibilities and apply to the FCA for approval for the individual, where appropriate.
- Ensure that the statements cover all prescribed responsibilities (if appropriate).

- Ensure Senior Managers are trained on the Conduct Rules and the Senior Manager Conduct Rules before 9 December 2019.
- Identify who is performing a certification function.
- Before 9 December 2020, assess whether such individuals are fit and proper and, if so, issue a certificate to that effect setting out the aspect of the firm's affairs in which the individual will be involved.
- Put in place systems and controls (including HR and IT systems) to ensure that:
 - An annual fit and proper assessment is carried out for Senior Managers and Certified staff.
 - All Senior Managers and Certified staff are trained on the Conduct Rules applicable to them by 9 December 2019 and that all other staff (excluding ancillary staff) are trained on the Conduct Rules by 9 December 2020.
 - Changes are updated in the senior management statements of responsibility and resubmitted to the FCA.
 - Prescribed information about Certified Staff is uploaded to the FCA Directory by 9 December 2020 and all changes are notified with seven days.



Timing and implementation

In December 2017, the FCA published a consultation paper addressing the transitioning of the SMCR to all relevant FCA firms. SMCR rules were published by the FCA in a policy statement in July 2018 and will come into force on 9 December 2019.

For the majority of firms, the FCA is proposing automatically to convert individuals approved under the Approved Persons Regime (APR) to the new regime. This means the majority of firms will not need to submit applications to convert existing approved persons to Senior Managers holding Senior Manager Functions.

The self-certification regime is given a year to bed down. The Conduct Rules will apply to all Certified staff from the date SMCR comes into force, but firms will have a year-long transition period to complete their fitness and propriety assessments and put certification paperwork in place.

For non-Certified staff, the Conduct Rules will apply following the year-long transition period, giving firms a further 12 months to train those staff.

The Senior Management Function (SMF) Regime

SMFs

Persons carrying out the following SMFs in Core SMCR Firms will need prior FCA approval.

Any of four “governing functions”:

- SMF1: Chief executive
- SMF3: Executive director
- SMF9: Chair
- SMF27: Partner

Any of two “required functions”:

- SMF16: Compliance oversight
- SMF17: Money laundering reporting officer (MLRO)

In addition to those SMFs applicable to Core SMCR Firms, persons carrying out the following SMFs in Enhanced SMCR Firms will need prior FCA approval:

- SMF2: Chief finance function
- SMF4: Chief risk function
- SMF5: Head of internal audit
- SMF7: Group entity senior manager
- SMF10: Chair of the risk committee
- SMF11: Chair of the audit committee
- SMF12: Chair of the remuneration committee
- SMF13: Chair of the nominations committee
- SMF14: Senior independent director
- SMF18: Other overall responsibility
- SMF24: Chief operations function

There is no territorial limitation on the scope of SMF: a person outside the UK may potentially hold a SMF. A person performing a SMF may hold more than one SMF.

Every person performing a SMF will need to have a “statement of responsibilities,” setting out the areas for which he or she is responsible. This will need to be submitted to the FCA as part of the SMF approval process and is likely to follow the same format used to persons seeking SMF approval under the existing regime.

Prescribed responsibilities

Persons approved to carry out an SMF must take on FCA “prescribed responsibilities” (PRs).

These responsibilities must only be performed by a person approved to carry out a SMF, but a firm is free to decide which of its persons holding a SMF should be responsible for each of them.

There are six PRs for Core SMCR Firms:

- PR1: Performance by the firm of its obligations under the senior manager’s regime, including implementation and oversight.
- PR2: Performance by the firm of its obligations under the certification regime.
- PR3: Performance by the firm of its obligations in respect of notifications and training of the Conduct Rules.
- PR4: Responsibility for the firm’s policies and procedures for countering the risk that the firm might be used to further financial crime.

- PR5: Responsibility for the firm’s compliance with Protection of Client Assets and Money (CASS) obligations, if applicable
- PR6: Responsibility for an authorised fund manager’s value for money assessments, independent director representation and acting in investors’ best interests.

There are seven further PRs for Enhanced SMCR Firms:

- PR8: Compliance with the rules relating to the firm’s responsibilities map.
- PR9: Safeguarding and overseeing the independence and performance of the internal audit function (in accordance with SYSC 6.2).
- PR10: Safeguarding and overseeing the independence and performance of the compliance function (in accordance with SYSC 6.1).
- PR11: Safeguarding and overseeing the independence and performance of the risk function (in accordance with SYSC 7.1.21R and SYSC 7.1.22R).
- PR12: If the firm outsources its internal audit function, taking reasonable steps to ensure that every person involved in the performance of the service is independent from the persons who perform external audit, including:
 - Supervision and management of the work of outsourced internal auditors.
 - Management of potential conflicts of interest between the provision of external audit and internal audit services.
- PR13: Developing and maintaining the firm’s business model.
- PR14: Managing the firm’s internal stress-tests and ensuring the accuracy and timeliness of information provided to the FCA for the purpose of stress-testing.

The FCA expects firms to allocate the prescribed responsibilities to an Executive Director or Partner, with the exception of PR9, PR10 and PR11, which should be allocated, where possible, to a Senior Manager who is a Non-Executive Director of the firm or a Partner who does not have management responsibilities.

Enhanced SMCR Firms will need to appoint a senior manager to have overall responsibility for every area, business activity and management function of the firm. Enhanced firms will also need to put in place “responsibilities maps”: a single document that will set out the firm’s management and governance arrangements.

Duty of responsibility

Each person holding a SMF will have a statutory duty of responsibility. This means that, if the firm breaks one of the FCA’s rules, the person performing the SMF responsible for that area could be held personally accountable if that person failed to take “reasonable steps” to prevent or stop the breach. The burden of proof for establishing the lack of reasonable steps remains with the FCA. However, prior commentary from the FCA has made it clear that doing nothing, in circumstances where reasonable steps requires something to be done, will not suffice.

When applying the duty of responsibility, the relevant statement of responsibility will be crucial in establishing the scope of an individual’s responsibility.

The Certification Regime

A certification regime will apply to those staff who do not carry out SMFs, but who carry out functions that involve, or might involve, a risk of significant harm to the firm or any of its customers (Certification Functions).

Firms will be responsible for certifying at least once a year that these people are suitable to carry out the respective Certification Function.

The following are proposed as Certification Functions:

- Significant management function (based on CF 29).
- Proprietary traders (also covered by current CF 29).
- CASS oversight function (current CF 10a).
- Functions subject to qualification requirements.
- Client dealing function.
- Algorithmic traders.
- Material risk takers.
- Anyone who supervises or manages anyone performing any a Certified Function (directly or indirectly) but is not carrying out a SMF.

The Certification Functions only apply where the firm has people in these roles. Therefore, it is possible that in very small firms there will be no one in the Certification Regime if there are only a handful of senior individuals (who will be carrying out the SMFs).

The conduct rules

Conduct rules will apply to persons carrying out SMFs and Certification Functions and also to all other staff (other than ancillary staff).

The conduct rules set out the expected behavioural standards and are similar to the existing Statements of Principle applicable to approved persons under the APR.

There are two tiers of rules: The first tier applies to persons carrying out SMFs and Certification Functions and other staff (other than ancillary staff), while the second applies only to persons performing SMFs:

First Tier – Individual Conduct Rules

1. You must act with integrity.
2. You must act with due care, skill and diligence.
3. You must be open and cooperative with the FCA, the PRA and other regulators.
4. You must pay due regard to the interests of customers and treat them fairly.
5. You must observe proper standards of market conduct.

Second Tier – Senior Manager Conduct Rules

SC1. You must take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively.

SC2. 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.

SC3. 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.

SC4. You must disclose appropriately any information of which the FCA or PRA would reasonably expect notice.

The FCA has proposed that the Conduct Rules apply to a firm's regulated and unregulated business, including any related ancillary activities.

Limited Scope Firms will be subject to the Conduct Rules. The only required SMF roles and required approval here are for persons carrying out functions falling under SMF16, SMF17 and SMF29 (Limited Scope Function, which is the same as the Apportionment and Oversight Function under the APR).

Prescribed responsibilities will not apply to Limited Scope Firms.

The Directory

The Directory is a public register maintained by the FCA.

Firms will be required to upload certain prescribed information about their Certified staff by 9 December 2020. Firms will be required to report leavers, joiners and other changes to information within seven days.

Conversion of individuals under the APR to SMCR

Core SMCR Firms and Limited Scope Firms

Individuals at Core SMCR Firms and Limited Scope Firms approved under the APR will be automatically converted wherever possible to the corresponding SMF, with no further action required by firms.

However, individuals moving from a current controlled function to a different SMF (for example a current CF1 director moving to a SMF1–Chief Executive role) will still need FCA approval and will need to submit a statement of responsibilities to the FCA.

In addition, a person approved under the APR as a CF2 currently acting a firms' non-executive chair will need to apply to carry out the SMF 9 chair function, though in this case will not need to submit a statement of responsibilities.

Enhanced SMCR Firms

Individuals at Enhanced SMCR Firms under the APR do not benefit from the automatic conversion to the corresponding SMF.

Enhanced SMCR Firms will have to notify the FCA who they want to assign to the relevant SMF, but they will not have to re-apply for approval if the proposed SMF can be mapped directly from the APR.

Enhanced SMCR Firms will need to submit:

- A "Form K" detailing all of the approved persons to be converted to SMFs.
- Statements of responsibilities for all of the SMFs included in the Form K.
- A responsibilities map.
- Prescribed forms for new or transferred individuals.

Self-Certification Regime

Firms will need to carry out the first certification of persons falling into the self-certification regime as “fit and proper” 12 months after the SMCR regime comes into force.

There is no need to obtain regulatory references for existing employees who will continue to perform the same role under the new regime.

Conduct rules

The conduct rules will apply to all persons carrying out SMFs or self-certification functions from the date that the SMCR comes into force (9 December 2019).

Other persons within the scope of the conduct rules (i.e. employees who are not ancillary staff) will not become subject to these rules until 12 months after the SMCR regime comes into force.

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