

CLIENT MEMORANDUM

Extension of the Senior Managers and Certification Regime by the UK's FCA

Does the SM&CR apply to my firm and what does it entail?

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AUTHORS

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Summary

On July 26, 2017, the Financial Conduct Authority (**FCA**) published a press release together with consultations which include its proposals to extend the Senior Managers and Certification Regime (**SM&CR**) to practically all regulated firms. In essence, the FCA intends that the SM&CR will apply to all firms offering financial services in the UK, including firms authorised in the UK and incoming branches of non-UK-authorised financial services firms, and will replace the current Approved Persons Regime.

The SM&CR has applied to banks, building societies, credit unions and Prudential Regulation Authority (**PRA**)-designated investment firms since March 2016, and the FCA now intends to extend its application to (re)insurers, other investment firms, asset managers and insurance intermediaries, among others.

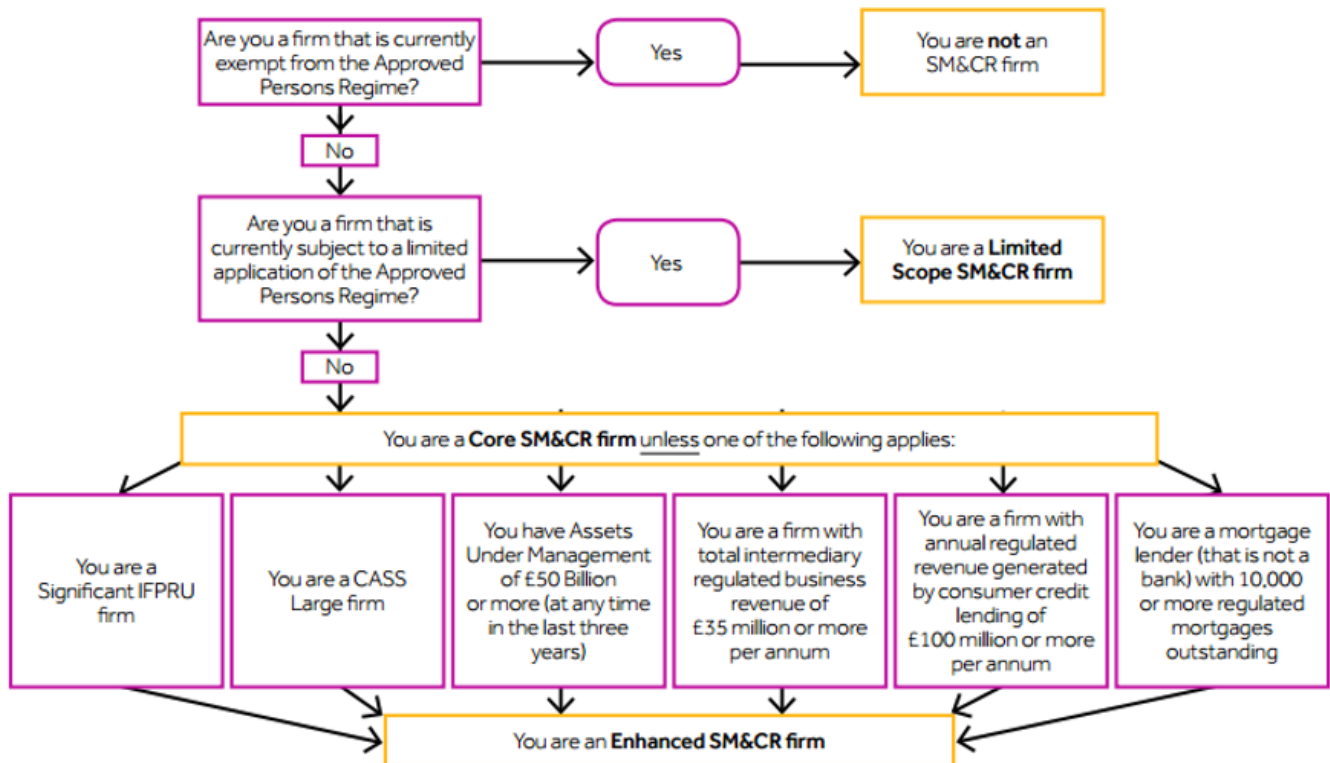
The regime will have a particular significance to the senior managers of the firms whose responsibilities fall within the SM&CR (**Senior Managers**). Senior Managers will be expected to take personal responsibility for their actions and should therefore take careful note of what the regime entails.

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Does the SM&CR apply to my firm?

The FCA consultation document provides a useful diagram for firms to use to determine whether and to what extent the SM&CR will apply. We have replicated this diagram below for reference.



To ensure that the regime is proportionate to all firms to which it will apply, a “core regime” of specific requirements will apply to most firms (**Core Firms**). In addition, for larger and more complex firms, an “enhanced regime” will apply with extra requirements; however, these extra requirements will apply to fewer than 1% of firms (**Enhanced Firms**).

In respect of firms who have limited permissions and are currently subject to a limited application of the Approved Persons Regime, the SM&CR will also apply but on a more “streamlined” basis (**Limited Scope Firms**).

The SM&CR will not apply to Appointed Representatives. The FCA notes that it will confirm how it will approach the SM&CR for Appointed Representatives in a follow-up consultation paper. However, principals of such Appointed Representatives, including the Senior Managers of such principal firms, shall remain fully responsible for ensuring that their Appointed Representatives comply with the FCA’s rules.

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Scope of the SM&CR

The SM&CR applicable to the remainder of financial services firms will not be identical to that which currently applies to banks, building societies, credit unions and PRA-designated investment firms. Whilst the same tools and principles will be employed, the new regime is intended to be flexible and proportionate to the different size and type of firms to which it will apply, since these firms will inevitably have different business models and governance structures.

There will be three main parts to the SM&CR which will apply to every firm:

1. *Five conduct rules.* These conduct rules will apply to all financial services staff within the firm, requiring individuals to: act with integrity; act with due care, skill and diligence; be open and cooperative with the regulator; pay due regard to customer interests and treat customers fairly; and observe proper standards of market conduct.
2. *Responsibility of Senior Managers.* The responsibilities of the Senior Managers will be clearly set out and, in the event that something goes wrong that is within a certain Senior Manager's purview, that person will be held personally to account. As with the current Approved Persons Regime, all Senior Managers will be approved by the FCA and appear on the Financial Services Register. Further details regarding the Senior Managers regime are set out below.
3. *Certification regime.* In addition to the regime for Senior Managers, under the certification regime at least once per year firms will assess and confirm the fitness, skill and propriety of those individuals who are not Senior Managers but whose jobs significantly impact customers or firms.

Focus on individual responsibility of Senior Managers

The FCA makes it very clear in its press release that the new regime is "*about individuals, not just institutions.*" Jonathan Davidson, Executive Director of Supervision – Retail and Authorisations at the FCA, has stated that the regime will "*ensure that individuals in financial services are held to high standards*" and that Senior Managers are "*accountable both for their own actions, and for the actions of staff in the business areas that they lead.*"

This clearly represents the shift in perspective of the regulator from the firm to the individuals that work within it and the Senior Managers in particular. In preparation for the introduction of these rules, firms will have to consider their management and governance structures to ensure that they are ready for the full impact of the SM&CR.

The FCA rules will establish certain roles within a firm as "**Senior Management Functions.**" All persons who perform Senior Management Functions will need to be approved by the FCA, as under the current Approved Persons Regime. Firms will also need to ensure that they satisfy themselves internally that Senior Managers are suitable to conduct their respective roles. The following Senior Management Functions will apply to all firms:

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- Governing functions
 - SMF 9 – Chair
 - SMF 1 – Chief Executive
 - SMF 3 – Executive Director
 - SMF 27 – Partner
- Required functions
 - SMF 16 – Compliance Oversight
 - SMF 17 – Money Laundering Reporting Officer
 - SMF 29 – Limited Scope Function (relevant to some Limited Scope Firms only)

However, a number of firms will not need to apply all of the Senior Management Functions outlined above. For example, a sole trader will not need to have any of the governing functions. Similarly, for limited permission consumer credit firms, if they are currently only required to have an individual carrying out the “Apportionment and Oversight Function” under the Approved Persons Regime, going forward they will only be required to appoint a Senior Manager to perform the analogous Limited Scope Function under the SM&CR. In this way, the regime should be commensurate to the size and complexity of each specific firm.

Each Senior Manager will have a document which sets out the matters for which they are personally responsible and accountable. There are certain specific responsibilities that a firm will need to give to its Senior Managers (referred to as the **Prescribed Responsibilities**), which are applicable to all firms (except Limited Scope Firms). Where something goes wrong in respect of a matter for which that Senior Manager is responsible, the FCA will look at whether the Senior Manager took “reasonable steps” to stop that error from occurring. As such, Senior Managers will need to ensure that there are robust lines of reporting within their business areas, such that they can inform themselves of all actions taking place that fall within the scope of their regulatory responsibilities. Without this, Senior Managers will find themselves personally accountable for matters of which they are not aware and could be subject to penalties.

For Enhanced Firms, there will be an “Overall Responsibility” requirement, whereby the firm must ensure that every activity, business area and management function has a Senior Manager responsible for it. This will include additional Senior Management Functions such as a Chief Finance Function, a Chief Risk Function and a Chief Operations Function, among others. Each Senior Manager will also be responsible for additional Prescribed Responsibilities. Such firms will need to have a “map” which sets out the firm’s management and governance arrangements to show how they meet these criteria.

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Next steps

All firms which are regulated by the FCA will need to pay close attention to the details of the FCA's consultation paper in order to establish if and to what extent the SM&CR will apply to the firm, its Senior Managers and its other employees. In particular, firms will need to review their current management and governance structures to ensure that they are ready for the full impact of the SM&CR. The Willkie team would be happy to address any questions that clients and friends may have on the new regime and how it will apply to your firm.

In addition, responses to the FCA's consultation on the extended application of the SM&CR are due by November 3, 2017. The Willkie team intends to provide input and we would be happy to consider and reflect any comments that clients and friends may wish to make on the proposals.

If you have any questions regarding this memorandum, please contact Joseph D. Ferraro (+44 20 3580 4707, jferraro@willkie.com), Nicholas Bugler (+44 20 3580 4704, nbugler@willkie.com), Andrew Tromans (+44 20 3580 4715, atomans@willkie.com), Henrietta de Salis (+44 20 3580 4710, hdesalis@willkie.com), or the Willkie attorney with whom you regularly work.

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