

Extending SM&CR – The devil in the details

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We have all now had a couple of months to enjoy the consultation papers published for Accountability 2, CP17-25 and CP17-26.

In this article I will highlight some of the key areas for firms to focus on when considering their response to these papers. I have avoided repeating a summary of the rules of the new regime, a lot of summaries have already been published but some areas are perhaps a bit less clear and deserve more attention.

I recently attended a briefing held by FCA for the benefit of professional services firms working with clients who would be impacted by the extension of the Accountability regime. This was a very useful session and similar (I understand) to the Regulated Firm briefings that FCA have also been running. I would strongly recommend attending one of these briefings near you, if at all possible.

For those who have not had chance to go to one, I will summarise below some of the useful clarifications and updates we received.

1) Send a Response

All the way back at the start of the Accountability initiative, the first formal Consultation Paper published was CP14-13, July 2014, which set out the concepts of Senior Manager Regime, Certification and Conduct Rules. We had to wait until March 2015, 8 months later, for the first draft of the resulting rules. The regulator

received approximately 70 responses to the initial consultation paper and a further 17 responses to the Transitional Arrangements CP. Given that this significant new world was going to affect over 1000 deposit taking firms the volume of this response from the industry was pretty poor.

The extension of SMCR is going to significantly impact approximately 350 'enhanced' firms and over 13000 'core firms'.

At the briefing FCA vehemently stressed that more than anything else, what they wanted was feedback to the CP.

Even if you or your firm don't want to publish a formal response and document answers to all of the questions asked, you can send any queries over interpretation or implications to the Consultation Response team. It will be useful feedback for them that you simply draw attention to the areas which are not clear or need more guidance and you should receive at least some additional clarity to help in your planning.

2) Technical Transitions Consultation

FCA confirmed that the Transitions Consultation Paper, which will set out the 'how' of the implementation of the SMCR Extension, including the timetable, will be published later this year but definitely not before this current consultation closes on November 3rd.

One positive note however was that FCA stated their intention for most Senior Managers to be automatically transferred over to the new regime, without the 'form based' Grandfathering process which Banks and Insurers had to go through for Accountability 1. There will be some exceptions, for example NEDs and some others, but for most firms this should remove a significant administration effort from the 'technical transition' project.

3) Appointed Representatives

At the same FCA Briefing, they confirmed that the current proposed scope of the new SMCR will not cover Appointed

Representatives (ARs) and therefore the Approved Persons Regime (APER) will persist for them. FCA suggested this was because there was some doubt that the current legislation in the Financial Services and Markets Act (FSMA) granted FCA relevant powers to apply the new regime to Appointed Representative firms. They acknowledged that this was not ideal and that they were consulting further and seeking subsequent changes to FSMA to allow SM&CR to be extended to replace APER for ARs.

This is very unlikely to happen in the same timescale as the implementation for everyone else, therefore, for a while Principal Firms will be subject to SM&CR but APER will persist for their ARs. The responsibility for ensuring ARs compliance with the requirements of the regulatory framework will remain firmly with the Principals.

This means that for a while at least, the CF30 role will persist alongside Certification, just like we have today for Bank staff vs. other sectors.

The potential confusion in the industry as a result could be significant. For example, it not clear if AR CF30 staff will remain on the FCA Register, or how the implications for Regulatory References will be resolved. It should be remembered though, that Accountability will eventually be extended to cover ARs, so Principals firms would be wise to consider the extension when designing their own solutions.

If your firm will be impacted by this issue, please include comments about these issues in your responses to the Consultation.

4) For Core firms – PR6

If you expect that your firm is going to be a 'Core' firm, then you probably have already had some initial discussions about Prescribed Responsibility No.6:

PR06 - "Responsibility for ensuring the governing body is informed of its legal and regulatory obligations"

This is probably the most commonly asked question across the firms that I have been engaged

with. Many Core Firms have been asking who is expected to take on this PR, with some citing that they have a Compliance Director who is not a lawyer and therefore not able to fulfil the 'legal' obligations.

At the FCA Briefing this exact question was raised and their response was very clear – they are **not** expecting firms to have or recruit formal legally trained resources in-house.

FCA went on to say ".....for Core Firms, looking at the probable populations of Senior Managers, it is likely to be someone like an Executive Director or one of the Partners, or it could be a Compliance officer who takes it on. We don't have a particular focus on who that role (the PR for Legal and Compliance) should be but it's got to be someone who can genuinely discharge that responsibility." ".....it was not intended to be more 'onerous' than the corresponding obligations for Enhanced Firms"

“At the briefing FCA vehemently stressed that more than anything else, what they wanted was feedback to the CP”

For Enhanced Firms, they confirmed that the current 'status quo' of their forbearance regarding Legal Function and General Counsel would persist under the extension of SMR until the results of the Discussion Paper had been finalised. See the link below:

<https://tinyurl.com/FCA-Statement>

FCA did take away that maybe more guidance around this particular PR would be welcomed but until then, it may be that 'Sharing or Dividing' this is a PR needs to be considered.

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meaning of the current guidance to change – they will review that it makes sense under the extended regime but there are no plans revisit the detail or modify the sense of it.

This is useful clarity, particularly where so many firms are seeking opinion about ‘Reasonable Steps’ and what it might mean. In essence, we can expect the current published guidance to continue to apply.

6) Certification

The Certification regime is going to apply to both Core and Enhanced Firms and it in itself contains several of the most complex elements of Accountability 2, down in the details. The following is a list of some of the key aspects of Certification that were challenging for Banking firms:

- ❑ Definition of ‘Roles’ subject to Certification
 - Particularly the Significant Management Function
- ❑ Definition of ‘Employee’
- ❑ Fitness and Propriety Assessments

- ❑ Regulatory References
- ❑ Breach Investigations and Reporting

There is clearly not time or space to cover these issues in detail in this article but if anyone is interested in discussing these details, please do contact me.

It is clear from the experiences in the Banking sector that successful implementation of the Certification Regime and the Fit and Proper assessment process belongs in the ‘Front Line’. It is not a back office or HR only responsibility.

Implementing SMR and Certification are intrinsically linked and need to work closely together. We are at the very early stages of the timeline and a long way from final rules or deadlines but projects responding to the CP need to be set up on the right footing.

SMR and Certification are all about the day to day ‘Behaviour’ of people in their roles – it is not an MOT, done once a year and forgotten.

Senior Managers will need support from Risk and Oversight monitoring of compliance with the new regime obligations.

The ‘devil is in the details’ and the history of this idiom is interesting. Although no one knows for certain where it originated or who first coined the phrase, the belief is that originally the phrase was ‘God is in the detail’. This seems to be a contradiction but probably is a deliberate difference born out of timing and attention!

If you think about the details in advance, give the details sufficient attention you can plan for them. If you work through the implications and consequences, from the details it is possible to create a great solution, which is efficient and effective.

You can create value out of getting the details right – in early 18th century you could justifiably claim that ‘God is in the Detail’.

If you don’t plan and consider in sufficient depth, details which appear insignificant may very well contain hidden problems that threaten the overall feasibility of your solution – the little devils!!!!



5) Duty of Responsibility and Reasonable Steps

On page 22, Section 4.25 of CP17-25, reference is made to a further consultation for guidance on the Duty of Responsibility. The section states that they expect the current guidance to apply to non-banking firms but that this will be reviewed in the technical ‘transitions’ CP later this year. FCA clarified at the briefing that they do not expect any material review of the contents or

- ❑ Certificates for Trainees
- ❑ Interaction with SPS processes
- ❑ ‘Territoriality’ Rules
- ❑ Definition of ‘Client Dealing’
- ❑ ‘Temporary UK Roles’ and ‘Emergency Appointments’
- ❑ Material Risk Takers
- ❑ ‘No Gaps’ rule
- ❑ Consistency of decision making and handling ‘exceptions’

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