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## Senior Managers and Certification Regime: Major changes on the horizon

### What is changing?

- From 9 December 2019, all FCA solo-regulated firms, as well as EEA and third country branches will be subject to the Senior Managers and Certification Regime (“SMCR”) which will replace the current Approved Persons Regime (“APR”).

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The SMCR aims to:

- make individuals more accountable for their conduct and competence;
- encourage staff at all levels to take personal responsibility for their actions;
- ensure firms and staff clearly understand and can demonstrate where responsibility lies.

Senior Managers will continue to be approved by the FCA. Employees that are not Senior Managers but are carrying out functions that could pose a risk of significant harm to the firm or its customers (“Certified Functions”) will now be assessed as fit and proper by the firm.

Almost all staff (including those who are not Senior Managers or “Certified Function” holders) will be subject to the FCA’s “Conduct Rules.”

### Why do these changes matter?

- Firms will be required to provide the FCA with a clearer picture of individuals’ responsibilities, which will establish a clear road map for enforcement action (and potentially significant fines and other sanctions) against individuals.
- Firms will also have new obligations to ascertain, certify and monitor the fitness and propriety of their staff on an ongoing basis, provide training to staff and hold their staff to high standards of personal conduct.
- Partners in private equity firms will also need to consider the conversion to SMF27 and how the Certification Regime applies to staff more widely, particularly given existing CF4s (who may not necessarily be considered SMF27 under the SMCR), are not “employees” under the certification regime. Responsibility mapping will be ever more important as PE firms and partnerships implement the SMCR rules. The changes may involve (amongst other things) amendments to employment contracts or the signing of side letters to reflect the importance of competent performance of the responsibilities outlined (as explained further below).

### What do firms need to do?

- Firms need to act promptly to identify individuals who will act as Senior Managers and the responsibilities that will be assigned to those individuals.
- Review activities in all jurisdictions and the influence exerted by individuals in other group entities (who may sometimes be located overseas).

- Identify staff members which need to be certified as fit and proper and put in place appropriate mechanisms to conduct certification assessments.
- Provide training to staff on their obligations under the FCA’s “Conduct Rules”.

### Which firms are impacted?

All firms currently authorised by the FCA but not yet captured by the SMCR rules ("solo-regulated firms") and EEA and third country branches of all FCA-regulated firms will be impacted by the extended SMCR. Firms will fall into one of three categories:

- “Limited Scope” firms – Firms currently subject to a limited version of APR including some consumer credit firms and insurance intermediaries, sole traders, oil and energy market participants, and internally managed alternative investment funds.
- “Core” firms – Firms with permission to carry on regulated activities will fall within this category (unless they are Limited Scope or Enhanced firms).
- “Enhanced” firms – Firms meeting one or more of the following criteria:
  - Significant IFPRU firms;
  - CASS Large Firms;
  - Firms with Assets under Management of £50 billion or more (calculated as a three-year rolling average);
  - Firms with current total intermediary regulated business revenue of £35 million or more per annum (calculated as a three-year rolling average);
  - Firms with annual revenue generated by regulated consumer credit lending of £100 million or more (calculated as a three-year rolling average); or
  - Mortgage lenders and administrators (that are not banks) with 10,000 or more regulated mortgages outstanding.

### Are any firms exempt?

The extended SMCR will not apply to payment services firms or incoming EEA firms that only provide cross-border services, since they will be subject to their own local requirements.

A different version of the SMCR is already in place with respect to banks, insurers and insurance branches.

### What will be required of firms?

The table below summarises the requirements on firms. Many of these arrangements may already be in place, and whilst firms (and the individuals within them) will in many cases be familiar with equivalent requirements under the APR, there are some significant new requirements and challenges associated with applying the SMCR. For example, although it may be apparent who a firm’s Senior Managers are, the boundaries between their respective responsibilities may be less clear.

In some cases, firms may find that individuals based in other group entities and/or outside the UK now need to be approved as Senior Managers.

Careful judgement will also be required when deciding whether individuals fall within the SMCR’s Certification requirements. One particular challenge is identifying individuals who are based outside the UK and/or who may be “employed” by a completely separate legal entity for contractual purposes whilst dealing with clients in the UK. Once individuals requiring certification are identified, firms will need to implement systems enabling them to assess fitness and propriety *at least* annually.

## THE UK SENIOR MANAGERS AND CERTIFICATION REGIME FOR SOLO REGULATED FIRMS: AN OVERVIEW

		Limited Scope firms	Core firms	Enhanced firms	
<b>SENIOR MANAGER CONDUCT RULES</b>	<b>INDIVIDUAL CONDUCT RULES</b>	<b>Senior Managers Regime</b>			
		Identify individuals occupying Senior Management Functions (“SMFs”) (“Senior Managers”)	Y <i>(Fewer SMFs for Limited Scope firms)</i>	Y	Y <i>(Enhanced firms must identify additional SMFs)</i>
		Assign Prescribed Responsibilities to Senior Managers	N	Y	Y <i>(Enhanced firms must assign additional Prescribed Responsibilities)</i>
		Prepare and maintain Statements of Responsibilities in respect of each Senior Manager	Y	Y	Y
		Conduct Criminal Records Checks on and assess fitness and propriety of each Senior Manager	Y <i>(Unless firm is a sole trader)</i>	Y	Y
		Prepare Responsibilities Maps setting out the firm’s governance arrangements	N	N	Y
		Design and implement handover procedures	N	N	Y
		Comply with requirements relating to regulatory references	Y <i>(Unless firm is a sole trader)</i>	Y	Y
<b>INDIVIDUAL CONDUCT RULES</b>	<b>Certification Regime</b>				
	Assess and certify at least annually the fitness and propriety of individuals performing particular “significant harm functions”	Y	Y	Y	
	Comply with requirements relating to regulatory references	Y	Y	Y	
	<b>Conduct Rules</b>				
	Train and monitor compliance with Conduct Rules by all other staff performing financial services roles	Y	Y	Y	

What will be required of Senior Managers?

Senior Managers are subject to a “Duty of Responsibility”. In practice, this means that they may be held accountable (and may be subject to enforcement action and a penalty) if they are found by the FCA not to have taken “reasonable steps” to prevent or stop the firm breaching regulatory requirements in their area(s) of responsibility. What “reasonable steps” are considered to be will vary between firms, roles and individuals. Following a long debate, the FCA recently confirmed that the heads of legal functions within firms will not require approval as Senior Managers (unless they also occupy another Senior Management Function) which will come as a relief for in-house counsel.

The FCA does not seek to prescribe what Senior Managers must do in order to discharge their duty. A key part of the implementation process for firms already subject to the SMCR has been engaging early with individual Senior Managers, to encourage them to give thought to how they make (and, at least as importantly, record) key decisions.

In addition to the FCA Handbook’s “Conduct Rules”, which will apply to all individuals performing tasks relating to the carrying on of regulated activities (in practice ruling out only ancillary staff such as cleaning, catering and security staff), Senior Managers have to comply with additional “Conduct Rules”. These are similar to those currently in place under the APR, with the important addition of a specific rule requiring Senior Managers to delegate effectively—a theme that has featured prominently in previous enforcement action pursued by the FCA.

What should firms do to prepare for the SMCR?

The FCA’s near final rules on the SMCR require approval by HM Treasury, so the 9 December 2019 implementation date is still subject to final confirmation.

The FCA will allow transitional periods for firms to put in place arrangements to comply with the extended SMCR. Specifically, firms will have 12 months to certify staff for the first time, although they will need to identify staff requiring certification by the implementation date. Firms must also train all Senior Managers and “Certified Function” holders on the FCA’s “Conduct Rules” (and Senior Manager “Conduct Rules” if applicable) by the implementation date, although they will have 12 months to train other staff.

The FCA has indicated that firms have until one week prior to the implementation date to submit regulatory forms and supporting documentation. This date may currently appear as a speck on the horizon (particularly given much more immediate issues presented by Brexit and other upcoming regulatory changes), but for many firms, substantial preparatory work will be required to identify Senior Managers and “Certified Function” holder populations and finalise, and in some cases negotiate, Statements of Responsibilities. Firms may wish to use the arrival of the extended SMCR as an opportunity to review and refine their governance arrangements, which may require more involved planning and revisions to key employment and/or corporate documents. With the significant expected work involved for many firms, we advise firms to begin work on their implementation plans as early as possible.

**Ropes & Gray are hosting a series of training roundtables with clients to discuss the challenges of SMCR implementation and lessons learned from the banks’ experience of implementation. If you would like to register your interest at our upcoming series of events, please email [Mandy.Leung@ropesgray.com](mailto:Mandy.Leung@ropesgray.com).**