

Senior Managers and Certification Regime (SM&CR) Update

In an astonishing eleventh hour U-turn, HM Treasury has announced the abandonment of the highly contentious presumption of responsibility for senior managers within banks. The Regulator will therefore continue to carry the burden of proof in regulatory investigations against senior managers. The presumption of responsibility is to be replaced by a new statutory duty of responsibility on senior managers to take reasonable steps to prevent a regulatory breach.

As predicted, it has also now been confirmed that the SM&CR will be extended across all regulated firms from 2018.

Key points

- SM&CR to replace Approved Persons Regime for wider financial services industry in 2018.
- Controversial presumption of responsibility on senior managers of banks replaced with a statutory duty of responsibility – with little (if any) change in substance of senior manager obligations / expectations.
- Directors (including non-executive directors (NEDs)) expressly brought within scope of conduct rules.
- Obligation under SM&CR to report breaches of conduct rules to the Regulator removed.

New statutory duty – déjà vu?

The burden of proving that a senior manager failed to meet the expected standards in an enforcement action will rest firmly on the Regulator, reflecting the current position. Senior managers will be hugely relieved – the presumption of responsibility was widely regarded as the most troubling and draconian aspect of the SM&CR, deterring some from taking up senior manager functions for fear of regulatory exposure.

The presumption of responsibility has been replaced with a “new” statutory duty on senior managers to take reasonable steps to prevent regulatory breaches in their area of responsibility. However, this duty appears to bear a very close resemblance to certain of the conduct rules underpinning the Approved Persons Regime and the new SM&CR for banks:

Statement of Principle 7 for Approved Persons

An approved person performing an accountable significant-influence function must take reasonable steps to ensure that the business of the firm for which he is responsible in his accountable function complies with the relevant requirements and standards of the regulatory system.

Senior Manager Conduct Rule 2

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.

In practical terms, it is unclear at this stage what, if anything, the new statutory duty adds to these conduct rules.

Application of conduct rules to directors/ non-executive directors

Under the SM&CR, certain NEDs (so-called “Notified NED”) did not fall within the scope of the conduct rules (and therefore effectively fell outside of the Regulator’s conduct jurisdiction). It appears that this “gap” is to be plugged so that the Regulator will be able to enforce directly against these NEDs as well as all other types of director - for example, where such a NED fails to act with honesty and integrity.

Extension of the SM&CR

As widely predicted, the SM&CR will eventually replace the “discredited” Approved Persons Regime for all other authorised firms – including: investment firms, asset managers, mortgage brokers and consumer credit firms. This is wider than the extension to firms active in the fixed income, commodity and currency markets recommended by the Fair and Effective Markets Review.

The framework replacing the Approved Persons Regime beyond the banking sector is to be similar to that applicable to banks. That is, the three tier framework comprising (in brief):

- **Senior Managers Regime** – requires advance approval by the regulators of individuals performing senior roles.
- **Certification Regime** – requires firms to assess the fitness and propriety of individuals in roles that are capable of causing significant harm to the firm or its customers (“certified individuals”).
- **Rules of Conduct** – apply to differing extents to senior managers, certified persons and certain other employees of a regulated firm.

Removal of obligation to report breaches of the rules of conduct

In a further unexpected concession, the Treasury has removed the requirement that firms report to the Regulator all known or suspected breaches of conduct rules by relevant employees. This development will come as something of a relief to the banks, many of which were grappling with the difficult operational aspects of this requirement.

Timing

The Treasury confirmed the implementation date for the SM&CR to banks and PRA-regulated investment firms remains 7 March 2016. However, this is now without the presumption of responsibility and the requirement to notify breaches of rules of conduct.

The Treasury intend to replace the Approved Persons Regime and roll out the SM&CR industry-wide during 2018.

Conclusion

In abandoning the presumption of responsibility, the Regulator has lost a key string to its enforcement bow. Without this, the SM&CR is similar to the Approved Persons Regime in that the burden remains on the Regulator to establish personal culpability. However, with its focus on Statements of Responsibility for senior managers and Responsibilities Maps, the SM&CR does have a degree more potency. In this way, the SM&CR requires additional up front clarity as to a senior manager's responsibilities, thereby removing some of ambiguity upon which individuals may have sought to rely in their defence under the current regime.

Action points

- Firms already preparing for the first wave of the SM&CR should review their implementation programmes to make necessary amendments. For example, it is likely that relevant changes will need to be made to (amongst other things):
 - training materials;
 - handbooks;
 - internal policies and protocols;
 - briefing packs; and
 - governance-related documentation.
- Most obviously, this will involve the removal of all references to the presumption of responsibility.
 - Firms subject to the regime as from 2018 might usefully:
 - consider establishing a cross-departmental working group to co-ordinate the implementation of the new regime, involving representatives from relevant areas such as HR, Risk, Secretariat and Compliance; and
 - monitor progress of the Bill and implementation consultations published by the Regulator.

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