



# Investment funds

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January 2017

## Senior Manager's Regime and its applicability to all regulated firms

**The FCA is consulting on extending the Senior Managers and Certification Regime (SM&CR) to all regulated financial services firms in 2018, which will include many managers of investment funds.**

The SM&CR was introduced by the FCA and PRA in March 2016 for deposit takers and certain PRA designated investment firms. The regime was intended to increase personal accountability and responsibility in an effort to address the criticisms made of the Approved Persons Regime (APR) by the Parliamentary Commission on Banking Standards (PCBS) when it looked into the causes of the financial crisis. Even though the regime was designed to try and address problems within banks, the Government has decided to extend the regime to **all** regulated financial services firms. However, and to acknowledge that the application of the full banking regime would be inappropriate in certain sectors, the FCA will be required to ensure that the SM&CR is applied in a proportionate manner.

Whilst the detail of how the regime will be extended will not become clear until the FCA concludes its consultation exercise, regulated firms will need to start planning for the implementation of the SM&CR. The current timetable envisages the regime going live in early 2018 and so firms will have limited time to meet the challenges that this significant change will throw up.

### Senior Managers

The senior managers element of the regime most closely mirrors the existing APR, primarily because this is the only aspect of the new regime which involves individuals seeking prior approval from the regulators before they can take up their post. There are a number of Senior Management Functions (SMFs) which an individual can be approved to perform. The FCA is unlikely to require firms to have a set selection of SMFs; instead, firms will be required to ensure that they have the right SMFs for their governance structure. However it is likely that, along with many board members, most senior executives will be caught by the regime .

The FCA is consulting on bringing heads of legal functions within the regime. The consultation closed on 9 January and a decision from the FCA is expected within a couple of months. The consultation indicated a preliminary view that the legal function will fall under an SMF and, if so, all legal function activity would then become directly regulated by the FCA.

Firms additionally will be required to allocate other specific responsibilities to the SMF holders, with these responsibilities set out

### Any comments or queries?

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in a Statement of Responsibilities (SoR) that should be reflected in **their contract of employment** (and so you should consider taking advice on what changes will need to be made to the relevant persons' employment agreements). The SoRs will need to track across to a Management Responsibilities map that is provided to the FCA.

All SMF holders have a Duty of Responsibility, which means that they have a heightened risk of being disciplined by the FCA. This also means that the heads of legal functions in FS regulated companies are going to have to do a much more extensive level of ongoing review and reporting on the operations of their function than they may previously have had to.

### The Certification Regime

When the certification element of the regime is extended, significantly more people will be directly regulated by the regulator than was the case under the APR. There is no pre-approval of individuals under the certification element of the regime; instead, firms are required to take responsibility for ensuring that all of these individuals are fit and proper to perform positions where they pose a risk of significant harm to the firm or any of its customers. Individuals working in HR, legal, compliance and audit are all considered to be within this scope (depending on their specific role) and a particular area of focus is likely to be on those staff having taken training which is demonstrably relevant to their role.

It is also possible that individuals working in outsourced providers may also come within the regime so outsourcing agreements may need review.

As with SMF holders, firms are required to assess the fitness and propriety of certification staff on an ongoing basis.

### Conduct Rules

Along with the rest of the APR, the Statements of Principles and Code of Practice for Approved Persons will be replaced under the new regime. The differences between the old principles and the new conduct rules are significant, with the primary change involving the inclusion of a rule requiring staff to **"pay due regard to the interests of the customer and treat them fairly"**.

In addition to the conduct rules applying to senior managers and individuals covered by the certification regime, the conduct rules will also apply to **all employees other than ancillary staff**. The FCA is likely to require firms to train their staff about the conduct rules, and even if it does not this would seem to be a prudent step if only because all individuals covered by the conduct rules could be fined for breaches of them.

### Regulatory references

One of the criticisms made by the PCBS was of the failure of the APR to prevent "rolling bad apples". The regulators have therefore sought to supplement the SM&CR with changes to the rules for regulatory references in the expectation that this will weed out the "bad apples" from financial services. When assessing the fitness and propriety of prospective employees, firms will need to request **regulatory references going back six years**. Accordingly, regulated firms will need to keep information going back six years about current and former staff so that they will be able to give fair and accurate references. One consequence of these changes will be to prohibit firms entering into settlement agreements with departing staff which conflict with their duty to provide such references. It also means that firms will need to review their disciplinary processes to ensure that they provide sufficiently granular information to support the firm's ability to give references.

### Consultation process

Whilst the fundamental elements of this new regime are unlikely to be abandoned by the FCA, there will be scope in the forthcoming consultation for firms to shape the detail of the new regime in their sectors. If you would like to discuss these changes including on how you might assess and report on your legal function under the new regime or if you have any thoughts which you would like RPC to make on your behalf as part of the consultation process, then please contact either your usual contact at RPC, Anthony Shatz or Marcus Bonnell.

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