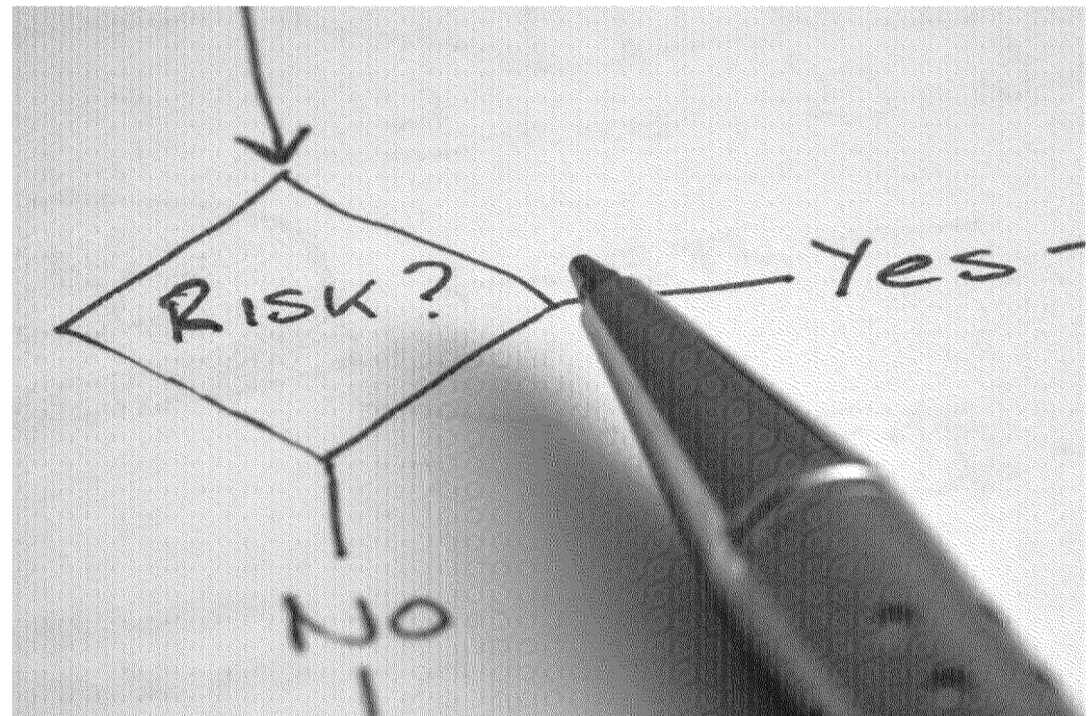


Linklaters

The changing regulatory environment

The impact of the senior manager and certification regime on the financial services sector



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11 January 2017

Background

- Financial services increasing importance to Post Office
- A highly regulated sector with increasing focus from regulators on customer outcomes and accountability
- Post Office is a unique structure
 - Appointed Representative for Bol and POMS
 - Largest Appointed Rep in UK
 - Agents not required to be Appointed Reps but operate under PO appointment
- Model likely to come under increasing scrutiny from regulators and from Principals as a result of the new senior managers regime and other initiatives

Objectives for this session

- 1) Understand challenges PRA/FCA authorised firms are facing with implementation of the Senior Managers and Certification Regime (SMCR)
- 2) Provide an overview of how the regime works and the implications for firms and individuals and likely impact on Post Office
- 3) Overview of individuals obligations under the Conduct Rules
- 4) Consider the expectations on senior managers and implications for wider compliance and conduct risk management
- 5) Discuss the likely implications for Post Office

Overview of SMCR

The SMCR is designed to enhance individual accountability, clarifying specific responsibilities of senior managers and expanding the range of persons who are subject to standards of conduct so as to impact individual behaviour and the culture within firms as a whole

Scope:

The SMCR captures individuals within:

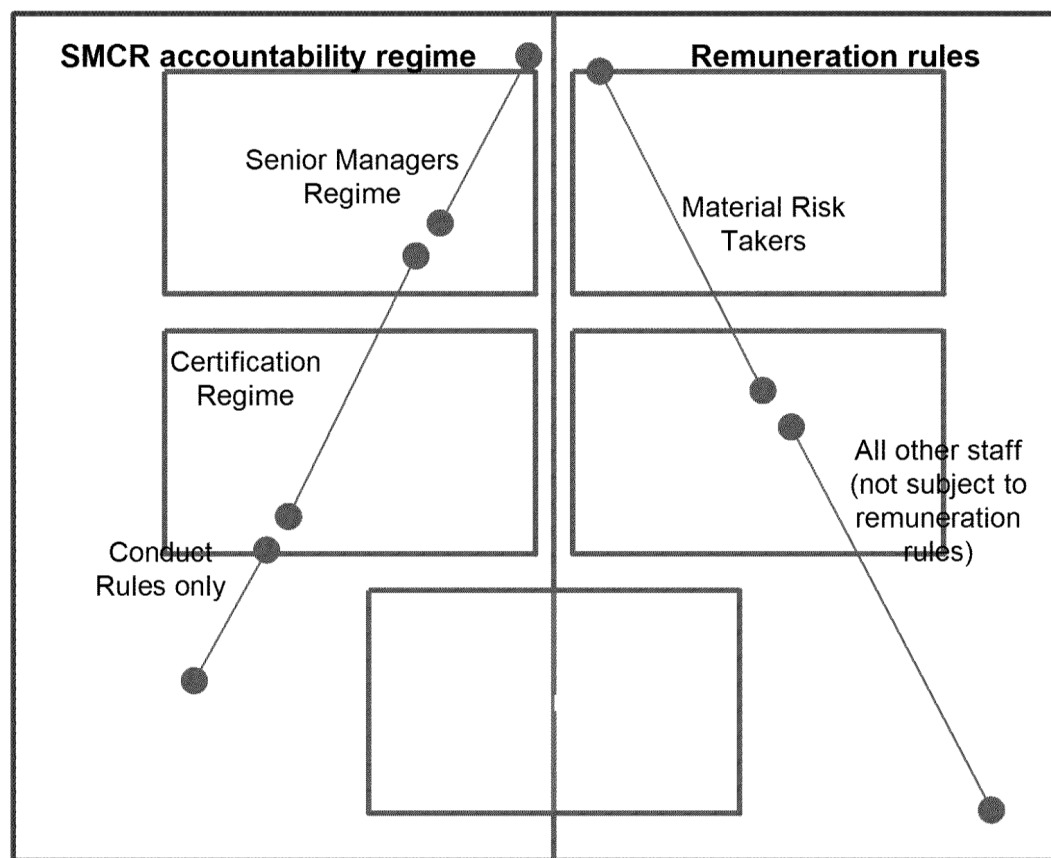
- Banks (including UK branches of foreign banks)
- Building societies
- Credit Unions
- PRA designated investment firms

The Senior Insurance Managers Regime (SIMR) covers insurers

Extension to **all authorised firms** planned for 2018 – Bank of England and Financial Services Act 2016

Part of a broader reform agenda:

- Changes to the remuneration rules
- Proposed changes to requirements for whistleblowing arrangements
- Proposals emanating from the Fair and Effective Markets Review
- Wider thematic review activity (e.g. on culture change and conduct risk programmes)



The new regime

Must be approved
by the regulators

**Certified
Persons**

Not approved by
regulators, bank must
certify fitness and
propriety annually

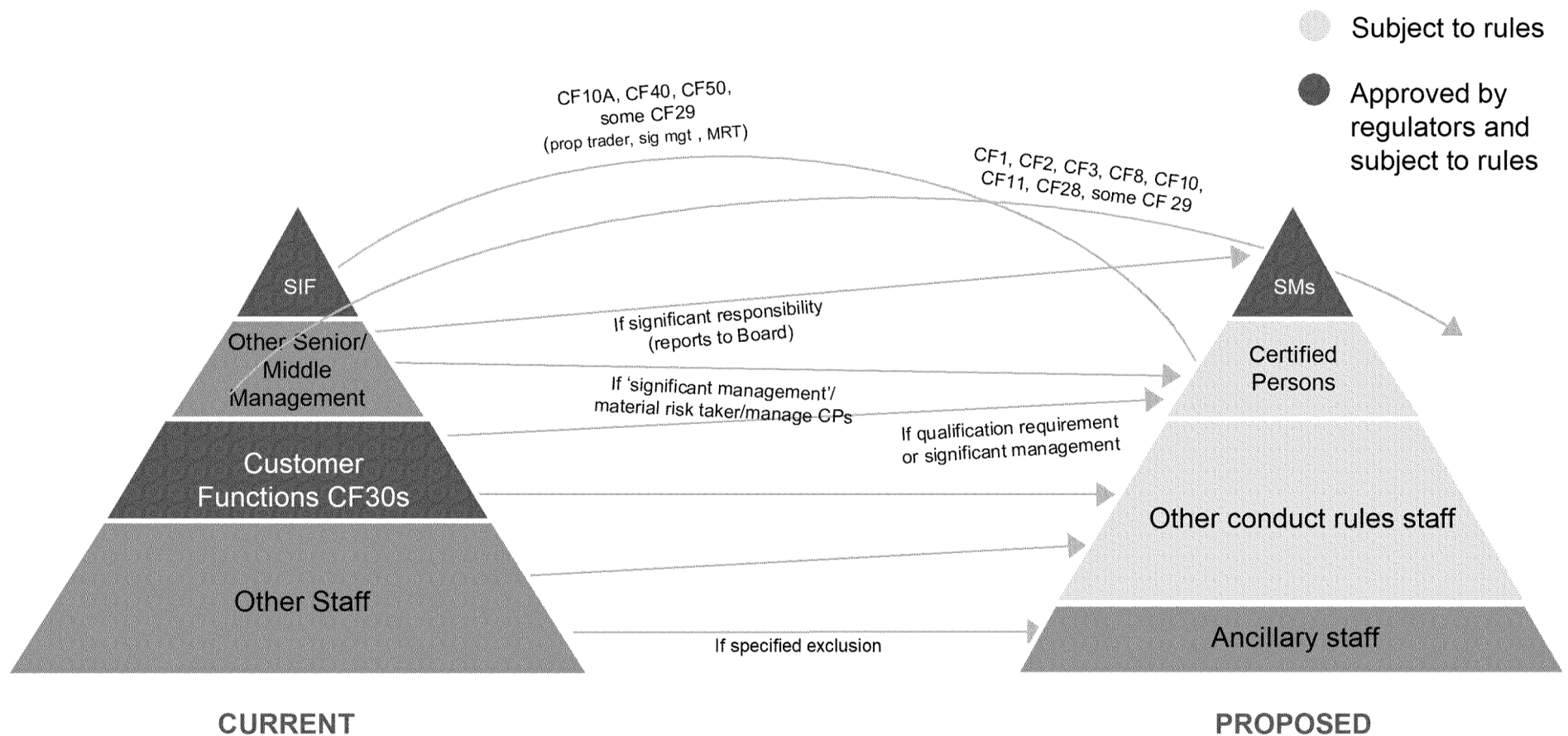
**Conduct
rule staff**

**Senior
Managers**

All three
categories will
be subject to
conduct rules –
and may be
fined for
breaching
them.

Not approved by regulators or subject to
certification. All employees except ancillary staff
are in this category.

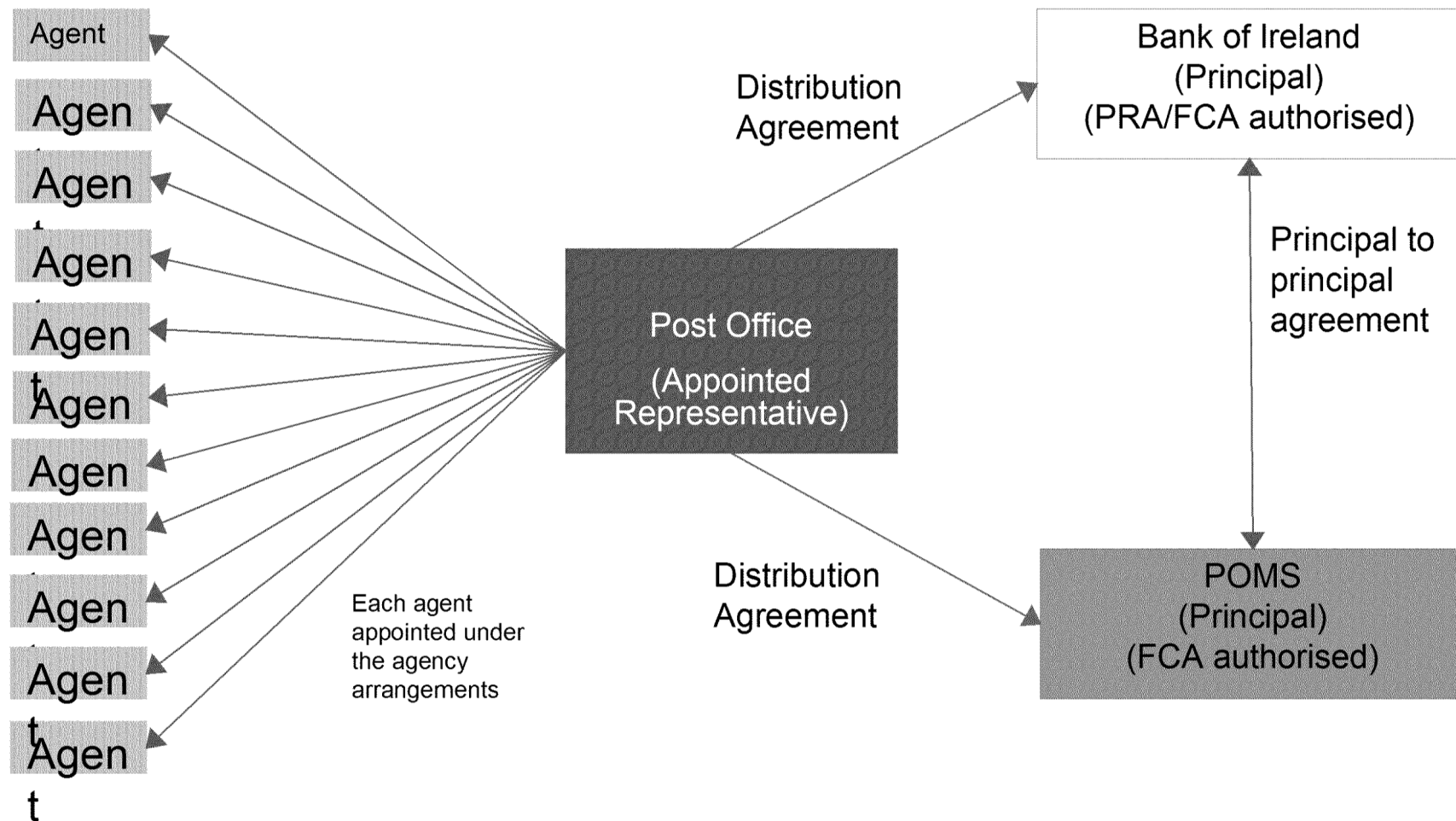
Comparison of current and new regimes



Senior Managers

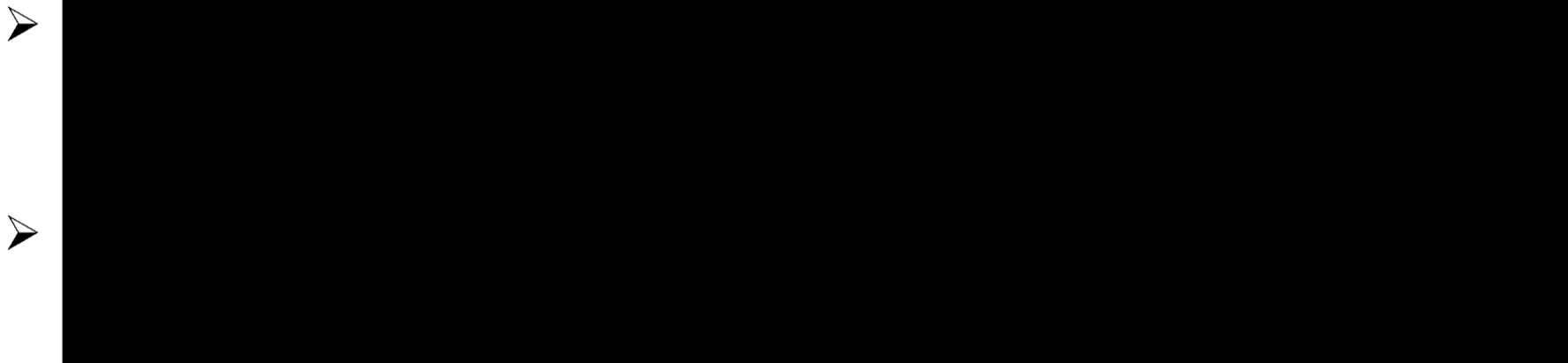
- Clear allocation of various designated senior management responsibilities.
- “Statements of Responsibilities” to record the allocation of responsibility to individual Senior Managers covering “*every part of a firm's activities, business areas and management functions*” (including unregulated activities).
- “Responsibilities Map” to be a single document describing the firm’s management and governance arrangements in order to demonstrate that there are no gaps in accountability.
- Where there has been a breach by the firm of its regulatory obligations in relation to an area within a Senior Manager’s remit, the regulator could take action against the Senior Manager for failing to take ‘reasonable steps’ to avoid a breach occurring or continuing.

Post Office structure



Implications

- Direct impact - implementation of SMCR for Appointed Representatives?
 - Approved Persons at Appointed Representatives?
 - Extension of conduct rules to staff at Appointed Representatives??



Conduct rules

- Will replace current Statements of Principle for Approved Persons (APER), and will apply to a wider range of individuals - Senior Managers, Certified Persons, and all other employees unless specifically excluded (e.g. facilities management, IT support, invoice and data processors, PAs etc).
- Firms must:
 - Notify all relevant individuals that they are subject to the Conduct Rules
 - Give all relevant individuals training on Conduct Rules – to include ‘deeper understanding of the specific rules which are relevant to their work’ (e.g. traders might be given tailored training on market conduct issues)
 - Notify the FCA of disciplinary action resulting from breaches of Conduct Rules

The Conduct Rules

The Conduct Rules reflect the core standards expected of staff working in impacted firms. Their broad application is intended to improve awareness of conduct issues through firms.

Individual Conduct Rules	Senior Manager Conduct Rules
Rule 1: You must act with integrity.	SM 1: You must take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively.
Rule 2: You must act with due skill, care and diligence.	SM 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.
Rule 3: You must be open and cooperative with the FCA, the PRA and other regulators.	SM 3: You must take reasonable steps to ensure that any delegation of your responsibilities is to an appropriate person and that you oversee the discharge of the delegated responsibility effectively.
Rule 4: You must pay due regard to the interests of customers and treat them fairly.	SM 4: You must disclose appropriately any information of which the FCA or PRA would reasonably expect notice.
Rule 5: You must observe proper standards of market conduct.	

Most of these are reflective of existing Principles and Code of Practice for Approved Persons. Although the highlighted rules are in one sense “new”, they are reflective of existing principles/guidance.

Liability consequences for individuals

Potential action against individuals	Potential consequences
Breach of the Conduct Rules by the individual <ul style="list-style-type: none"> All “employees” (excluding ancillary staff) will be required to comply with the general Conduct Rules Senior Managers (and persons carrying on the role of a Senior Manager without being approved) will additionally be subject to the Senior Manager Conduct Rules 	Fines <ul style="list-style-type: none"> Typically calculated having regard to the individual’s remuneration earned during the period of the breach No cap on the fine No insurance / firm indemnity possible
Being knowingly concerned in a breach by the firm of the rules applying to the firm <ul style="list-style-type: none"> This is an existing ground on which the FCA and PRA can take action against approved persons, but under the new regime will apply to Senior Managers and all employees 	Ban, suspension or limitation to regulatory approval <ul style="list-style-type: none"> E.g. 2 year suspension, imposition of conditions / time limitation Measures taken will depend on the nature of the misconduct For example, if the misconduct reveals that the individual is no longer fit and proper, a ban from carrying out any function in the financial services industry might be imposed.
Presumption of responsibility (Senior Managers only) <ul style="list-style-type: none"> If a regulatory breach occurs in an area for which a SM is responsible, the SM will be presumed guilty of misconduct unless s/he can show that they took such steps as they could reasonably be expected to take to prevent the breach occurring/continuing (the ‘presumption of responsibility’) 	Public censure / reputational risk <ul style="list-style-type: none"> Public disclosure of fines and breach/misconduct

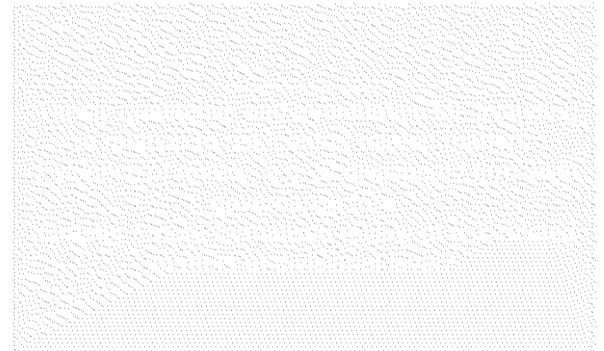
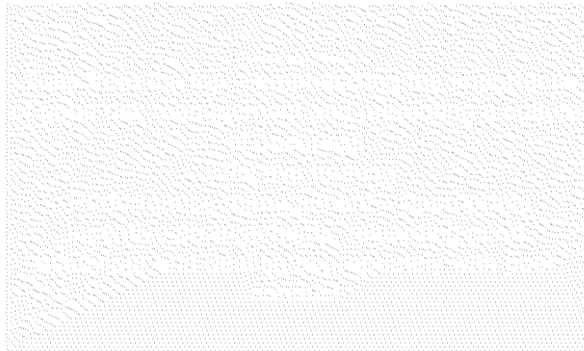
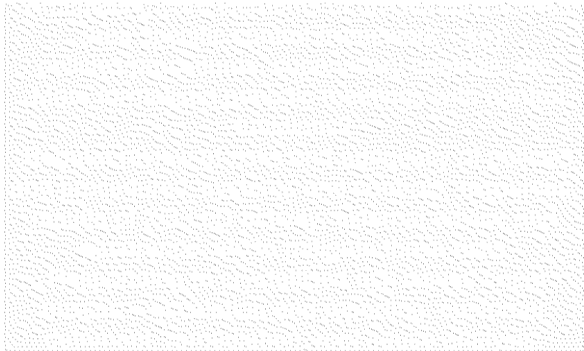
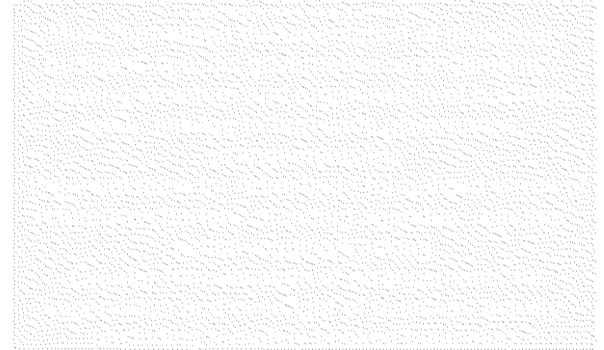
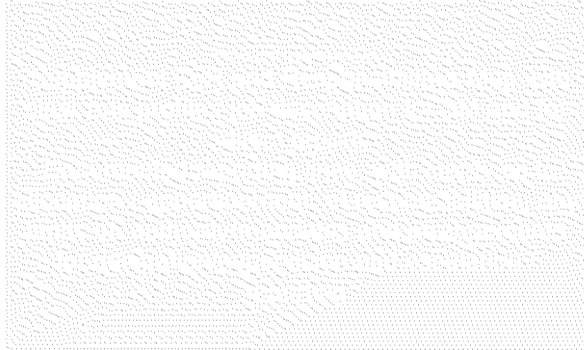
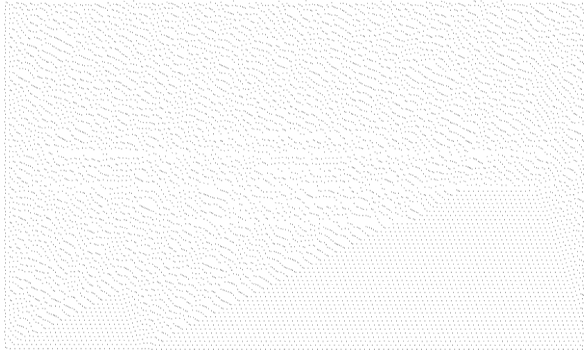
“Reasonable steps” for senior managers (1)

- Are there clear organisation charts and job descriptions in place showing reporting lines, allocation of roles and responsibilities and scope of authority (risk limits, signing authority, etc)?
 - Have you clearly delegated and apportioned your responsibilities to your direct reports?
 - Are you and your team clear on what they are and are not responsible for? Who do you rely on from a business execution and control oversight perspective?
 - If people have dual reporting lines, how do you make clear what this means in practice?
 - Has responsibility for all areas of the business under your control been clearly assigned/allocated? Do you have sufficient headcount / resource in place?
 - How do you ensure your team understand their responsibilities in relation to risk management and regulatory compliance, and monitor/report/escalate matters to you in a timely manner?
- You are not expected to be an expert in relation to every aspect of the business and you can delegate responsibility. Where you do delegate, you are not obliged to re-perform the tasks of your delegate BUT you retain regulatory responsibility for the matters that you have delegated. You must therefore ensure that any delegation is clear, effective and appropriately overseen:
 - Delegate to people who are sufficiently senior with the right skills, knowledge, capacity, competence and experience – are the staff in your team suitable and competent to perform the tasks delegated to them?
 - Ensure delegates are properly supervised and monitored
 - Put in place clear reporting lines so that issues can be escalated where necessary
 - Test and challenge the information received from delegates and other experts / specialists – “*trust but verify*”. Gain independent assurance (whether from control functions or third party experts) or obtain further information/evidence where necessary.
 - Track and monitor the progress of actions taken by delegates – regular reports on progress
 - Performance management and review – re-allocate tasks and replace people where necessary
 - Escalate to your line/functional management where appropriate.

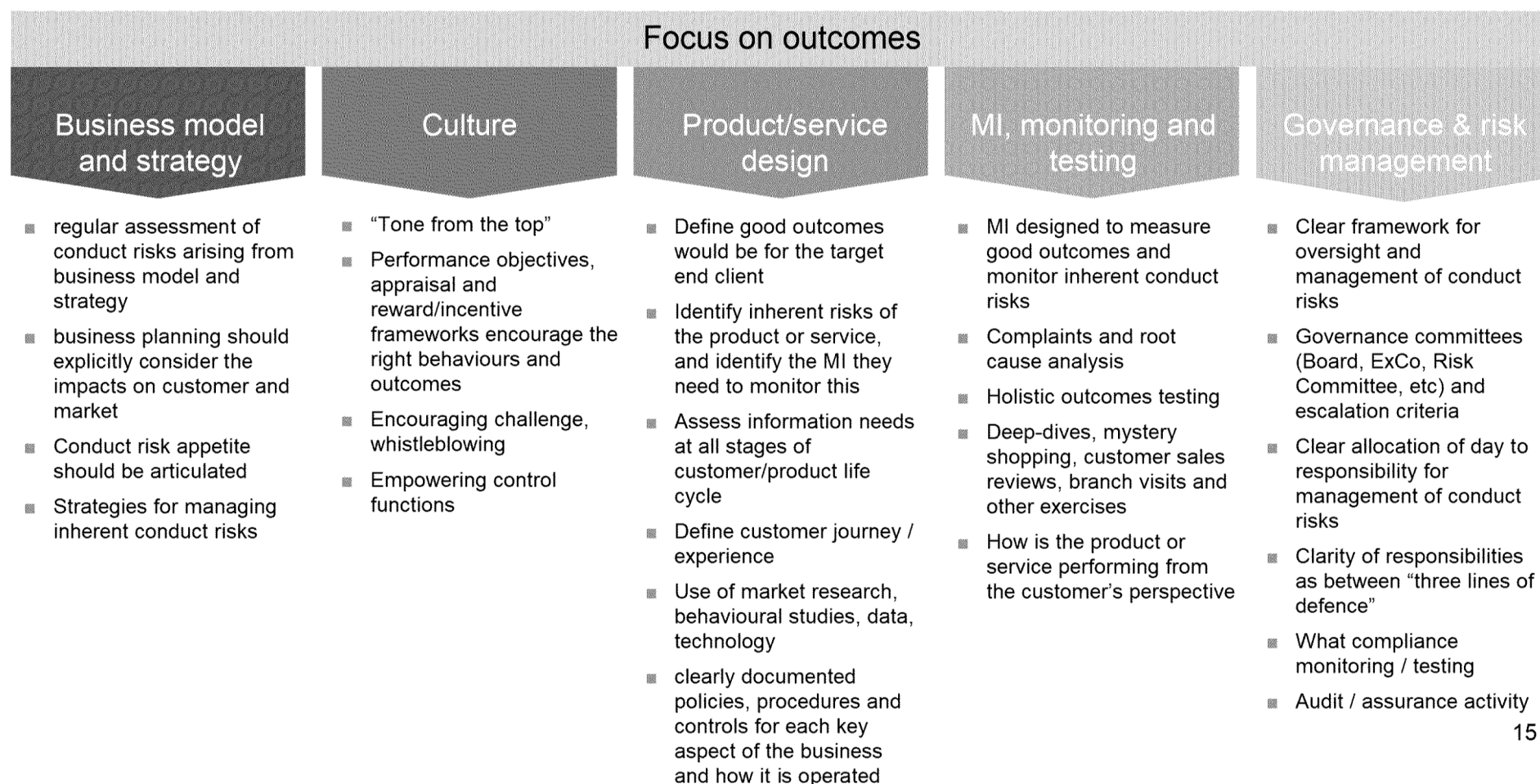
“Reasonable steps” for senior managers (2)

- Do you understand the firm’s risk management frameworks, and your particular responsibilities within those frameworks?
 - What are the key risks relevant to the business? E.g. Operational risks, legal risks, market risks, credit risk, counterparty risk, fraud / financial crime risks, liquidity risks, reputational risks?
 - Where are these risks identified? How are they controlled?
 - What are the policies and procedures that are relevant to your line of business?
 - What are the controls that are in place to ensure adherence to those policies and procedures?
 - What front office controls do you operate to ensure adherence? Consider operational risk controls, four-eye checks, segregation of duties, authorisation levels, trading limits, BAU supervisory controls, MI and reporting
 - Have your team been adequately trained on these policies, procedures, systems and controls, and on their personal responsibilities?
 - What mechanisms do you have in place for identifying and escalating breaches, considering their root causes/wider implications and taking action to address them?
 - What second and third line of defence / external assurance activity is undertaken to support management / monitoring of these risks? Consider – Financial Control, IT, Operations, Risk, Legal, Compliance, etc. Is further monitoring or assurance necessary or appropriate?

Establishing a possible framework for compliance



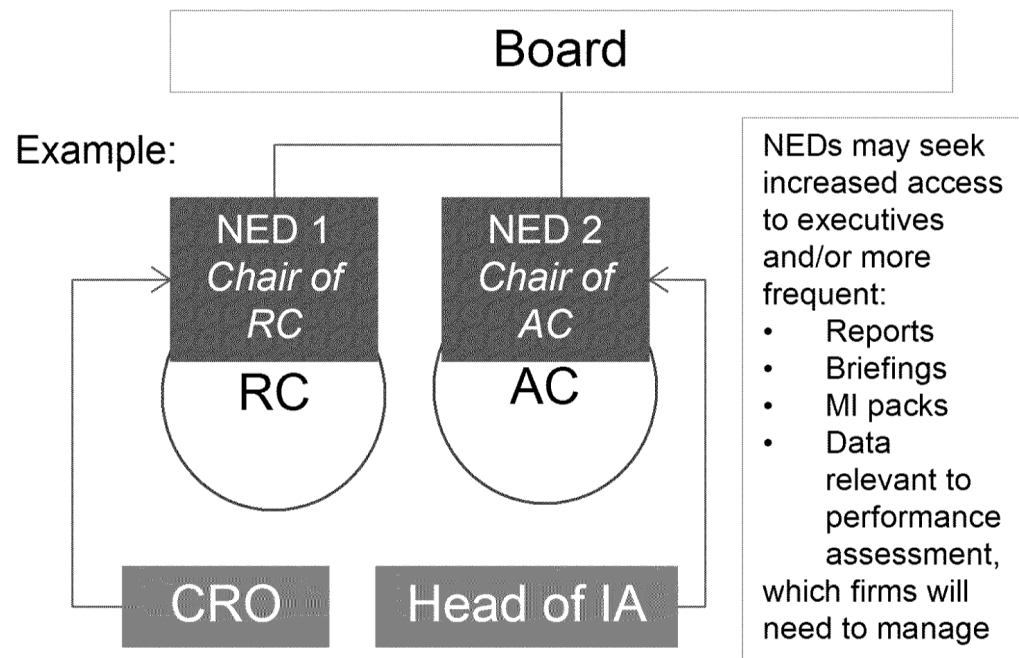
Conduct Risk Management



Non-Executives

The application of the SMR to NEDs does not impute 'executive like' responsibilities to NEDs but crystallisation of responsibilities for committees, and requirements in relation to the performance assessment of executive managers, may cause NEDs to re-assess the scope of their role and the tools they have at their disposal

- > Corporate governance principles articulate the importance of maintaining a clear division of responsibility between executives, who have responsibility for running the business, and the Board (including NEDs) who have oversight responsibilities
- > The SMR respects this distinction in the rules applicable to NEDs; however as NEDs, supported by the Office of the Chair, formulate explicit plans to discharge their responsibilities, they may consider that additional information/management access is required to perform their role
- > Demands for a 'ringfenced NED budget' and access to, e.g. independent legal advice, may also increase
- > Whilst equipping NEDs to discharge their responsibilities, it will be important for firms to ensure that NEDs neither compromise the responsibility of executive management nor their independence



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