



Morgan Lewis

**SMCR:  
TOP TIPS FOR IMPLEMENTATION  
AND KEY PRIORITIES FOR 2021**

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# Presenters



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# Before we begin

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# Senior Managers and Certification Regime (1)

- Senior Managers and Certification Regime (SMCR) comprises of:
  - Senior Managers Regime
  - Certification Regime
  - Conduct Rules
- SMCR introduced to **reduce harm to consumers** and **strengthen market integrity** by:
  - Encouraging staff to take personal responsibility for their actions
  - Improving conduct at all levels
  - Making sure firms AND staff understand and demonstrate who does what

# Senior Managers and Certification Regime (2)

## Senior Managers Regime

- Senior Managers who perform key roles (Senior Management Functions) will need **PRA or FCA approval** before starting roles and to be **certified once a year**
- Every Senior Manager needs to have **statement of responsibilities** that says what they are responsible and accountable for
- Firms need to assign specific responsibilities to senior managers, known as **prescribed responsibilities**
- Solvency II and large non-directive firms must provide **responsibilities maps** setting out responsibilities of their senior managers



# Senior Managers and Certification Regime (3)

## Certification Regime

- Applies to employees whose role means it is possible for them to cause **significant harm** to firm or customers
- Do not need FCA or PRA approval, but firms must certify they are **fit and proper** to perform their role at least once a year

## Conduct Rules

- Set **minimum standards** of individual behaviour
- Apply to almost all employees who carry out financial services activities or linked activities
- Senior Managers have additional Conduct Rules that they must comply with



# PRA: SMCR evaluation

Report published 16 December 2020



## Fitness and propriety

Supporting higher standards; supervisors are using to hold senior individuals to account



## Growing trust and confidence

Initial nervousness of SMCR has reduced as practitioners have grappled with system



## Impact on pay

Pay is being adjusted in response to adverse events; unclear extent influenced by SMCR



**% of SMs reporting positive impact on behaviours**

**94%**



**% of firms reporting positive impact on behaviours**

**96%**



## PRA: Integration of Conduct Rules

- 95% of PRA firms reported they had integrated conduct rules into HR and recruitment practices at least most of the time
- Small percentage of PRA firms said rules **occasionally** or **rarely** integrated
- Where integrated? Handbooks, codes of conduct, company values, and employee appraisal processes.

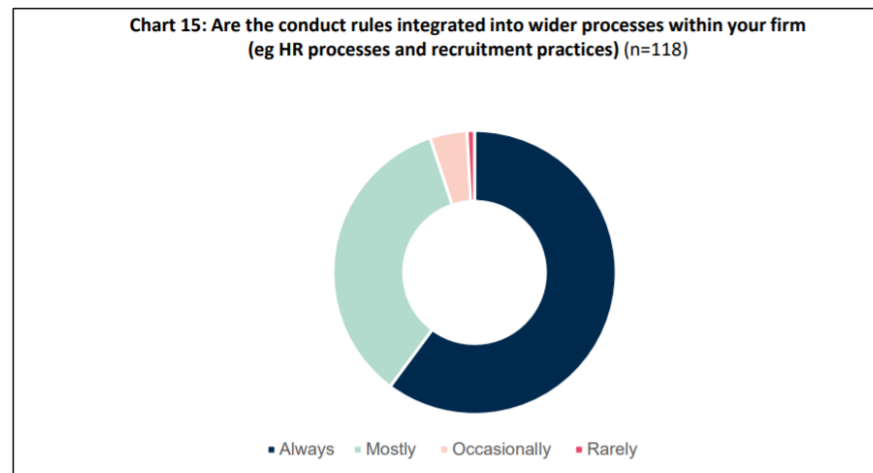


Chart 15 shows the proportion of firm Governance functions that consider the conduct rules to be integrated into wider processes within their firm (eg HR processes and recruitment practices).

Source: PRA "Evaluation of the Senior Managers and Certification Regime December 2020"

# PRA: Reporting breaches of Conduct Rules

PRA queries level of reporting over last 4.5 years (to October 2020)



## “Modest” Numbers

PRA says it is “difficult to form an estimate as to what constitutes an appropriate level of notifications, but the number of notifications received to date appears modest.”



## Senior Managers

**16 notifications  
to PRA**

**(approx. 7,850 PRA SMFs)**



## Certification Regime Staff

**104 notifications  
to PRA**

# PRA: Regulatory references

1

## Quality of references

- 85% of firms thought references were “mostly” or “always” of sufficient quality to inform assessment of individual’s suitability
- Insurance industry less confident than Banking industry

2

## Uncertainty

- Some firms cautious about their utility
- Some stakeholders noted the challenges of deciding what information to include

3

## Nervousness

- About hiring individuals with adverse comment on their reference
- Sensitivity of employees to comments on their references

4

## Overly punitive?

- SMCR not established to eliminate all mistakes or errors of judgment, especially as individuals can learn from these
- Case for PRA to engage stakeholders to determine if danger that references being used in ways that are “unnecessarily punitive”

# PRA: Recommendations

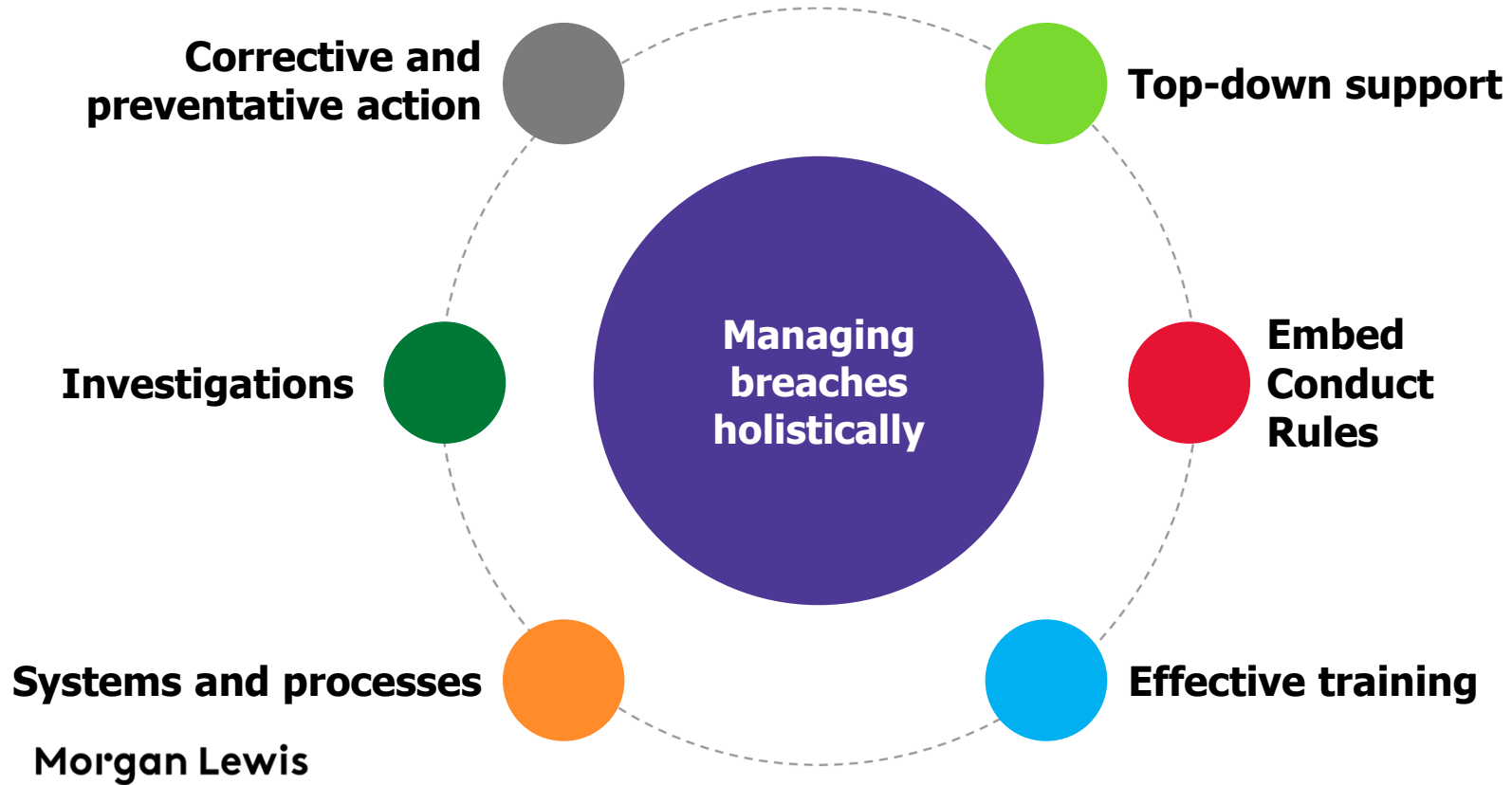
“There were some requests for further guidance on the threshold of conduct breach reporting and the level of materiality required, including the suggestion that the regulator could benchmark practices to enable more consistency”

## Recommendation

“Examine the scope for clarifying expectations related to misconduct reporting in notifications and regulatory references”

PRA to continue to review statistics on conduct rule breach reporting “and to use relevant communications to remind firms of the requirements”

# Holistic approach



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# FCA Statements



- **3 April 2020:**
  - FCA published statement of expectations for solo-regulated firms in light of COVID-19
  - FCA published joint statement (with PRA) for dual-regulated firms
- Firms were given extra flex to deal with staff shortages and reduce COVID-19 burden, e.g.:
  - Flexibility to furlough non-mandatory SMFs
  - No need to re-approve furloughed Senior Managers on return
  - Modification by consent for solo-regulated firms (until 30 April 2021)
- Regulators now say firms have adapted to COVID-19. Application of SMCR should return to normal. Some flex ended **7 January 2021.**

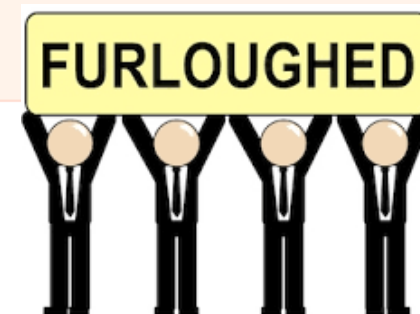
# FCA Statement for SOLO-Regulated Firms (1)

## Furloughed Staff

- Little change from FCA's April statement regarding furloughed staff
- Furloughed Senior Managers do not need re-approval on return
- Prescribed Responsibilities of furloughed Senior Manager should be re-allocated to another
  - If firm appoints temporary replacement under 12-week rule, Modification by Consent allows re-allocation even if they are not a Senior Manager
- Greater flexibility to furlough non-mandatory SMFs

**Note: required functions (i.e. Compliance Oversight, the MLRO officer and the Limited Scope Function) should only be furloughed as a last resort**

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# FCA Statement for SOLO-Regulated Firms (2)

## Statements of Responsibility

- FCA statement (3 April 2020):
  - Flex: SoRs did not need updating for any temporary changes due to COVID-19
- Flex ended 7 January 2021
- FCA now expects firms to apply notification requirements as normal
- FCA does not expect firms to now submit updates re: changes before **7 January 2021** but does expect clear documentation

## Senior Management Temporary Arrangements

- Previously: 12-week rule modified so unapproved individuals could cover absent Senior Managers for up to 36 weeks
- Modification by consent available (for now) to firms; firms should notify FCA of modifications.
- **30 April 2021:** Firms will no longer be able to consent to modifications and all modifications will end.
- Firms should document changes on SoRs and Responsibilities Maps (if applicable).



# FCA and PRA Statement for DUAL-Regulated Firms (1)

## Notifications about changes to Senior Manager responsibilities

- **April 2020:** regulators expected firms to resubmit relevant SoRs as soon as reasonably practicable but understood may take longer
- **Current position:** firms should submit SoRs as normal using Form J



## Notifications about temporary arrangements

- **April 2020:** FCA & PRA were gathering evidence on whether 12-week rule likely to give dual-regulated firms enough flex to deal with temporary absences of SMF as a result of COVID-19
- **Current position:** as before, firms can use 12-week rule to deal with temporary SMF vacancies. No extension to 12-week rule

# FCA and PRA Statement for DUAL-Regulated Firms (2)

## COVID -19 response

- Firms do not need to designate single SMF to be responsible for COVID-19 response
- Firms should consider which SMFs are better suited to aspects of firm's COVID-19 response
- Some aspects may sit well with the Chief Operations Function (SMF24) (if applicable)

## Furloughing SMFs

- Individuals performing mandatory SMFs should only be furloughed as last resort
- Firms should re-allocate mandatory/ required responsibilities of furloughed SMFs among other SMFs, or if relying on the 12-week rule, to an interim SMF
- Unless furloughed SMF is leaving, they will not need to re-approval on return but must remain fit and proper
- Firms must document reallocation of responsibilities of furloughed SMFs in SoRs, Management Responsibility Maps and internal docs

## Certification requirements

- Firms must continue to take reasonable steps to complete annual certifications of employees due to expire while pandemic restrictions in place
- FCA expects firms to have adapted to pandemic restrictions and complete requirements on time

# Monitoring and Surveillance (1)

- **11 January 2021:** FCA published expectations on recording telephone conversations and electronic communications in remote setting
- Firms should continue to comply with recording obligations in SYSC 10A
  - Take reasonable steps to record telephone conversations and keep copies of electronic communications of in-scope activities

## Risks arising from remote working

- Increased use of unmonitored apps, e.g. WhatsApp (FCA focus area)
- If apps used for in-scope activities on business device, should be recorded and auditable
- Firms should review policies and have rigorous monitoring regime
- Senior managers must establish right culture and governance within firms

## Monitoring and Surveillance (2)

- Must record telephone conversations/electronic communications of:
  - activities relating to performance of in-scope activities
  - communications intended to lead to such activities



### **Robust policies**

- Policies must be up-to-date (adapted for home-working) and meet recording rules
- ID telephone conversations and electronic communications subject to recording requirements and have procedures to follow where breach
- Consider whether policies for the use of privately owned devices provides sufficient scope for effective recording



### **Training**

Firms should provide training to staff if new policies are introduced or new technologies used

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# SMCR Implementation Deadlines (1)

- Deadline for solo-regulated firms to complete first F&P assessments postponed until **31 March 2021**
- FCA also extended deadline until **31 March 2021** for:
  - date Conduct Rules come into force for staff not Senior Managers or Certification Staff
  - date by which relevant employees must have received Conduct Rules training
  - submission of info about Directory Persons to FS Register

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MARCH 2021						
Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
28	1	2	3	4	5	6
7	8	9	10	11	12	13
14	15	16	17	18	19	20
21	22	23	24	25	26	27
28	29	30	31	1	2	3

## SMCR Implementation Deadlines (2)

- Certification Regime
  - Firms can still issue certificates during the **certification transitional period** (ending 31 March 2021)
  - Certificates issued during the transitional period effective for 12-month period
- Training in advance of Certification Regime implementation deadline
  - Employers need to train managers ASAP so can recognise potential F&P issues
  - Do not wait to remove staff who are already certified but no longer fit and proper





## SMCR Implementation Deadlines (3)



- Conduct Rules
  - With increased remote working, firms may need to adapt Conduct Rules training to ensure it can be delivered electronically
  - FCA expects to provide further guidance on training
- Information about Directory Persons
  - FCA setting up new public register with information on regulated individuals
  - Solo-regulated firms must submit Directory Persons data by **31 March 2021**
  - FCA has already published details of some certified employees (where firms have submitted by 9 December 2020)

FCA envisages most firms **won't need to rely on extension** and were encouraged to meet the original deadline (9 December 2020)

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# Stop the problem, before it happens

Firm culture is under ever-increasing scrutiny. Culture is considered to be at the heart of ethical lapses.

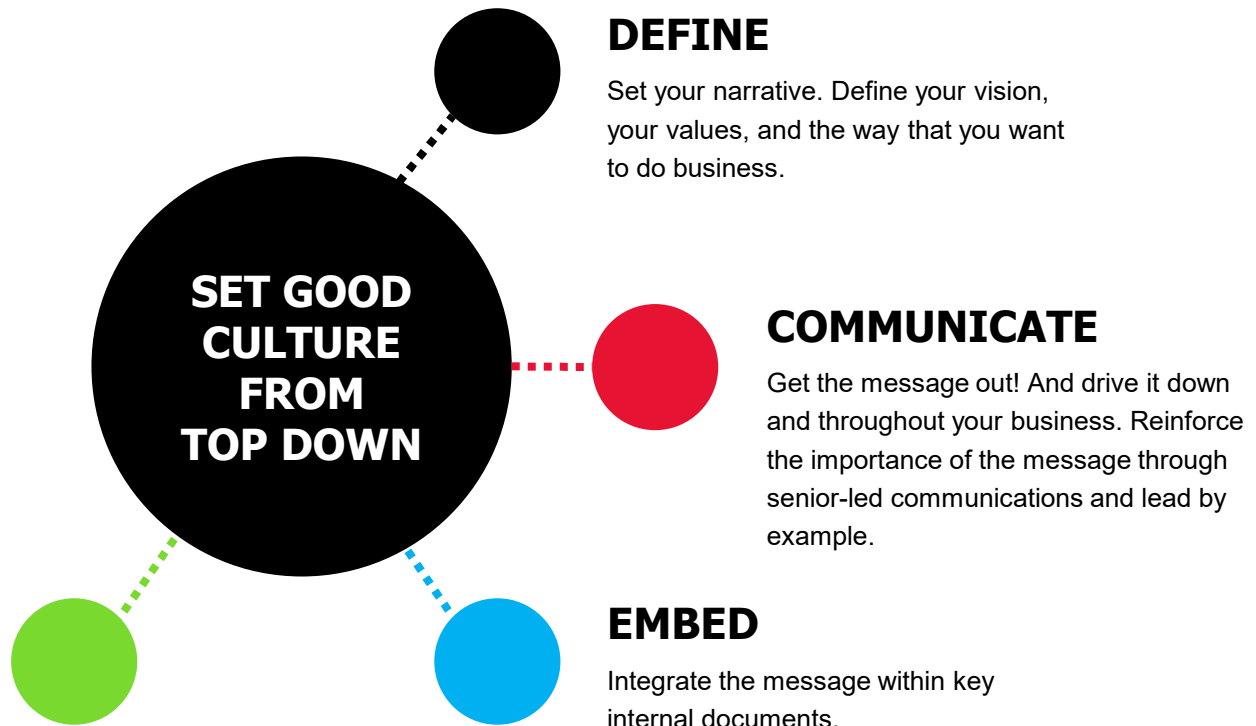
Good culture must be established and set at the very top.

## TEST RISK CULTURE

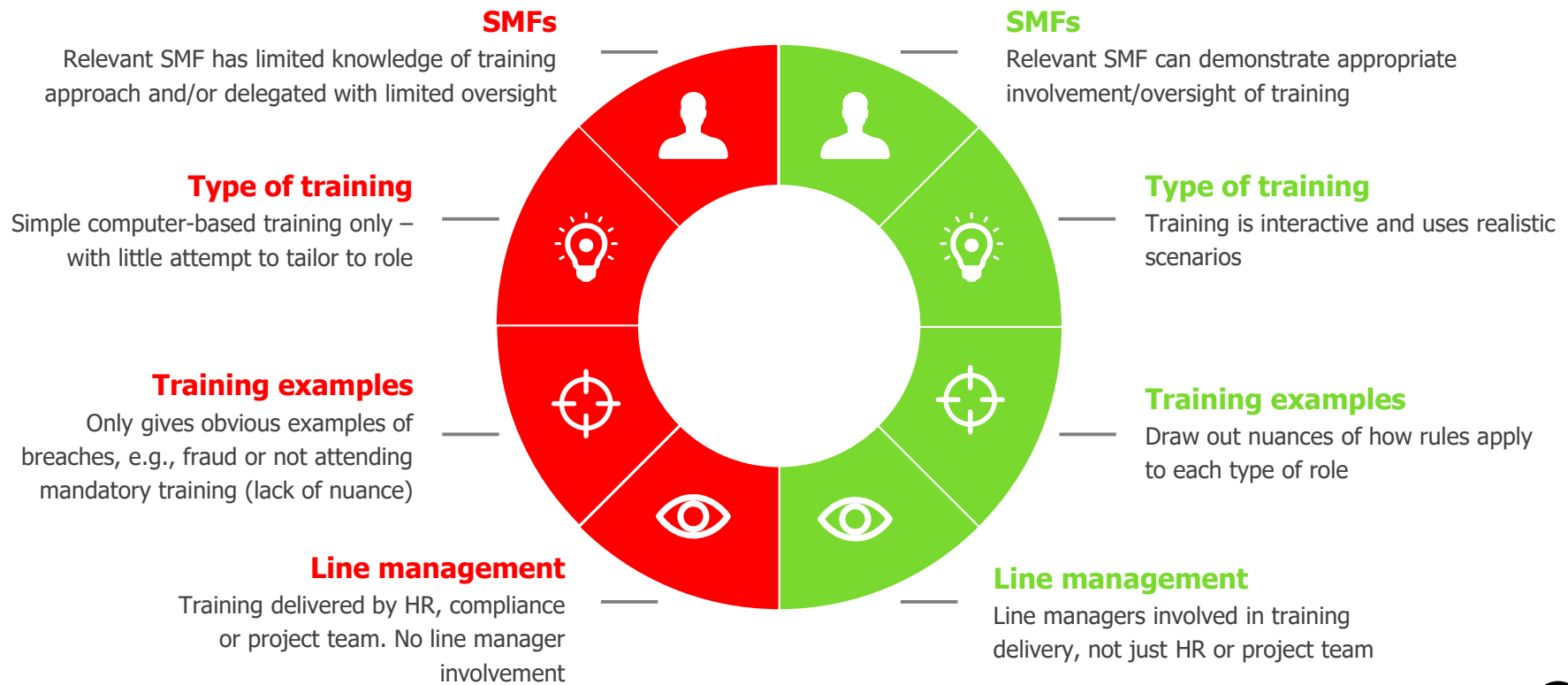
Consider:

- commitment of leadership
- information sharing
- willingness to escalate threats
- willingness to learn from mistakes
- structuring of incentives
- effective governance structures

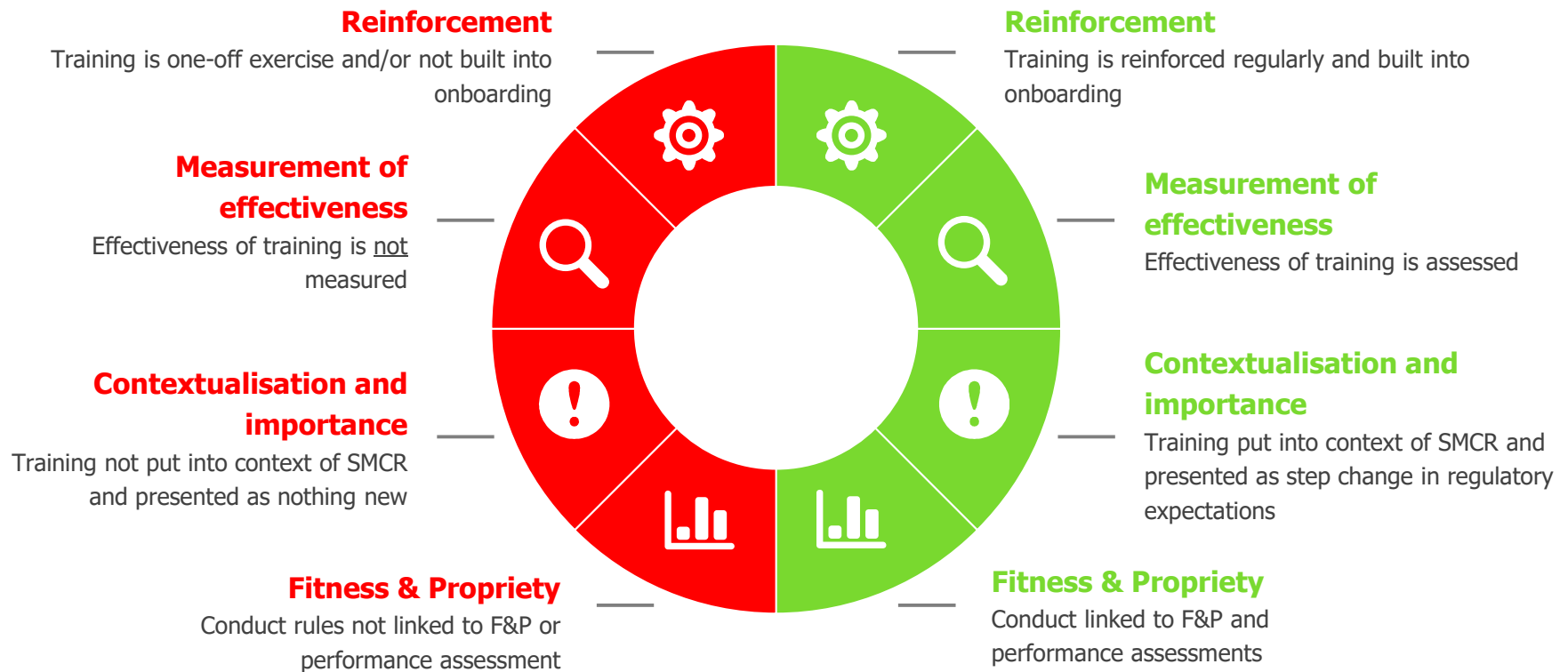
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# Delivering effective CR training: don'ts and do's



# Delivering effective CR training: don'ts and do's



## Key watch areas for the FCA (1)

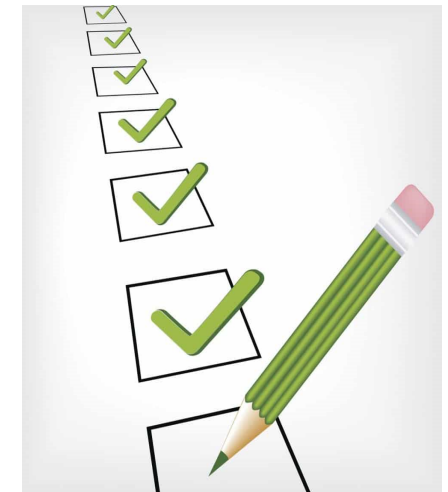


- Sexual harassment, discrimination, bullying and other personal conduct issues, especially as people return to workplace
- FCA recently banned 3 individuals from working in FS for non-financial misconduct outside workplace. Followed criminal prosecution for serious sexual offences
- FCA has indicated it will increase focus on how firms deal with non-financial misconduct by employees within and outside workplace

FCA has previously noted the handling of non-financial misconduct is indicative of firm's culture

## Key watch areas for the FCA (2)

- Present sufficient information regarding financial misconduct to management so management has full picture of risks, performance and conduct
- Assess how you deal with non-financial misconduct
- Proactively consider the types of non-financial misconduct that would trigger F&P and Conduct Rule breach (re-)assessment
- Train staff on the importance of conduct and behaviour within and outside workplace
- Include financial and non-financial metrics in assessments



# Investigating conduct rule breaches



Be clear on the process – identify any ambiguity early



Think wide: could the issue suggest broader concerns?



Engage the right stakeholders early



Avoid silo approach



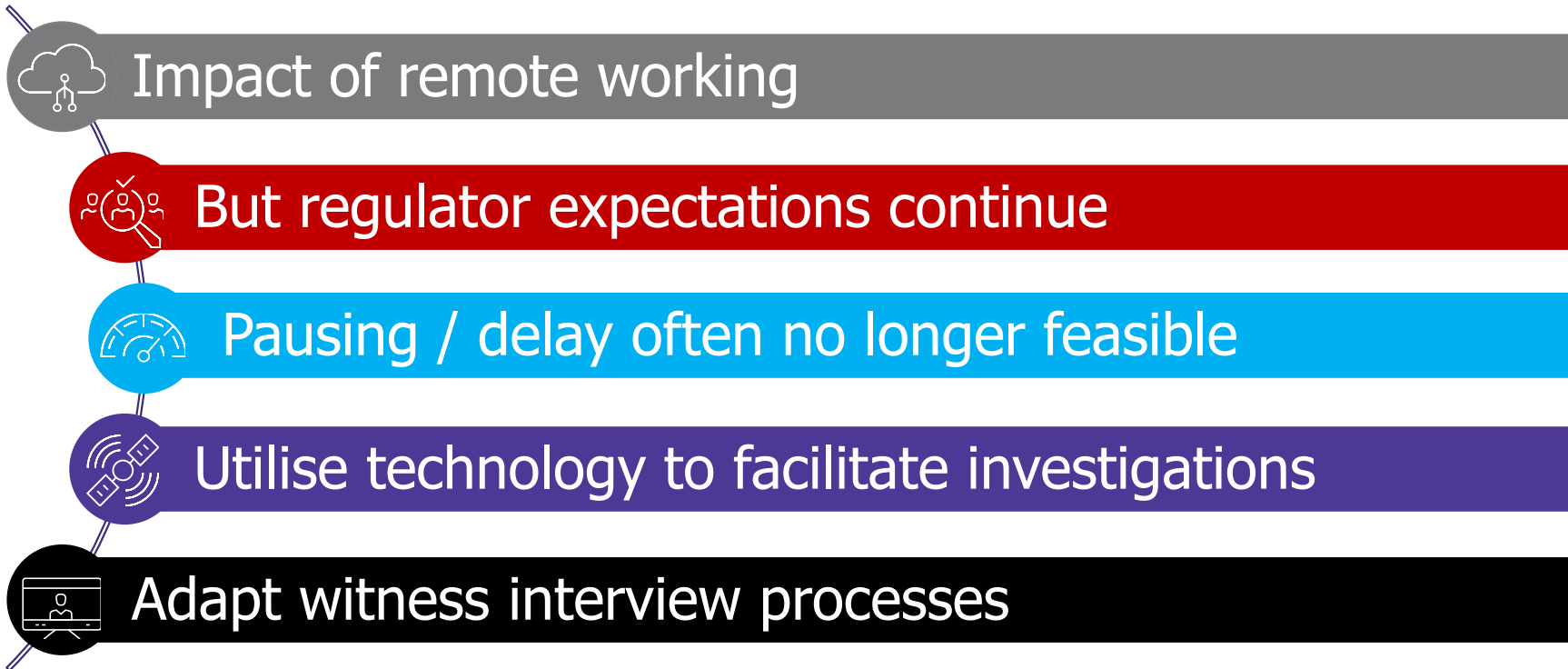
Assemble the right team



Always think: “How will this look later on?”



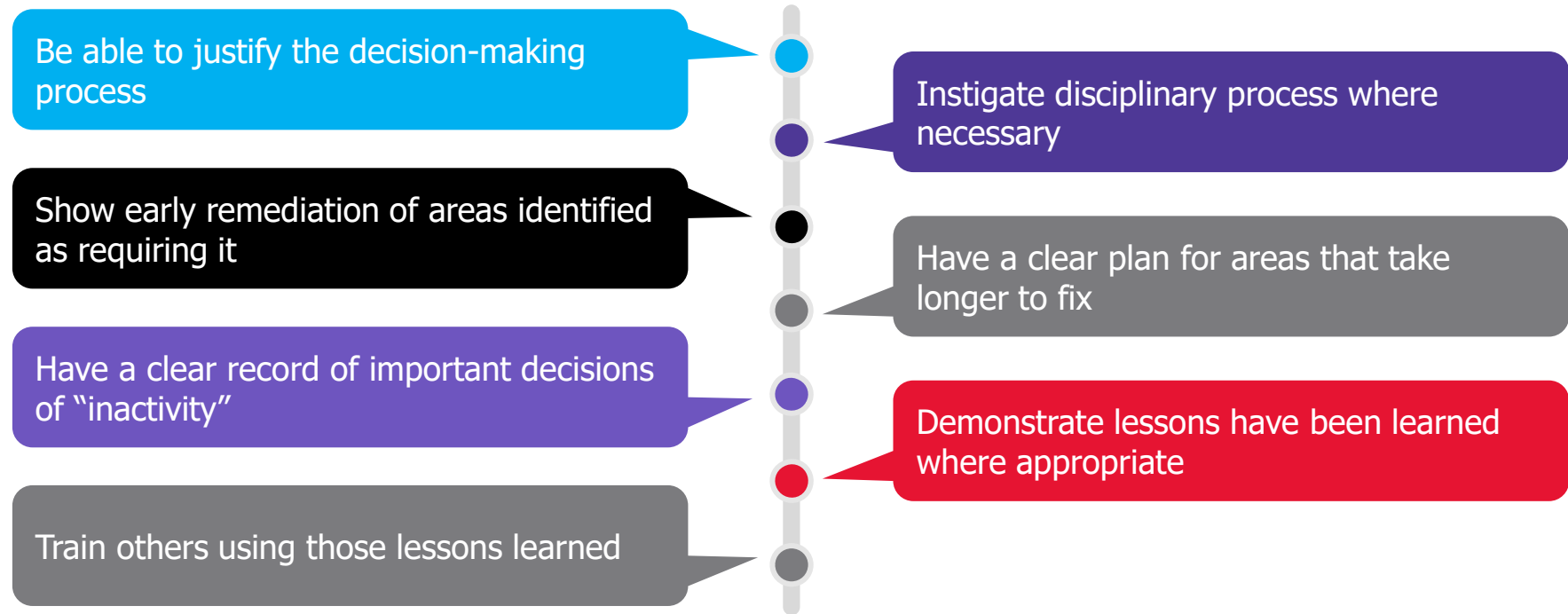
# Pandemic challenges



# Mitigating regulatory risks

- 1** Early-stage assessment wherever possible
- 2** Remember the audit trail
- 3** Be clear on what (and what not) to document at the outset
- 4** Recognise own failures and shortcomings
- 5** Record justifications for decisions and resolutions
- 6** Be alert to senior stakeholder conflict
- 7** Show the integrity of the process

# Corrective and preventative action



# Notifications to regulator

*For solo-regulated firms (SUP 15.11)*



## Senior Managers

Breaches by Senior Managers must be reported on Connect using Form D, or Form C where no longer performing a senior management function.

Notification should be made ASAP and within 7 business days.

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## Other than Senior Managers

Breaches by other individuals (e.g., certification employees or other conduct rules staff) must be reported annually. See right.

FCA has published a webpage on annual reporting requirement:  
<https://www.fca.org.uk/firms/senior-managers-and-certification-regime/rep008-solo-regulated-firms>



## The annual report

Called REP008. To be completed and submitted using Gabriel.

Firms must submit the report annually even if there have been no conduct rule breaches resulting in disciplinary action.

# Regulatory reference issues



Must request references from all previous employers in last 6 years for Senior Managers, Certification and non-approved NEDs

Provider must include details of disciplinary action due to Conduct Rules breaches, any findings that person not F&P, and any other information relevant to assessing F&P

- How much detail should you include?
- Should employee have a chance to comment?
- What to say if employee leaves before process completed?

Risk of claims (e.g., employment claims, negligent misstatement, deceit, defamation)

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# Practical issues arising from the pandemic (1)

- Substantial shift away from previous working norms
- Regulated firms must fulfil compliance obligations while many employees are working remotely
- Remote working challenges:
  - SMCR compliance processes may need to be adapted, especially if they rely on multiple individuals across different departments and offices
  - Managers may need to find new methods of discharging delegation and oversight duties
  - Firms may need to update policies and refresh training to reflect new remote working environment
  - Important to maintain an open dialogue with staff, especially re returning to office



## Practical issues arising from the pandemic (2)

- Culture challenges
  - Maintain good and open culture (especially important in the current climate)
  - Staff may disregard rules if feel not being monitored or supervised at home
- Training challenges
  - Think carefully about the different roles performed by staff; generic online training on the Conduct Rules may not achieve goal
  - Consider how to monitor whether individuals have completed training as opposed to simply 'flicking' through the pages without reading them





## Practical issues arising from the pandemic (3)

- Firms have statutory duty to provide safe place of work
  - Carry out suitable and sufficient risk assessments to identify risks
  - Mitigate identified risks
- Follow relevant government guidance to ensure workplace is safe once employees return
- Risk of H&S claims if employees feel appropriate steps not taken by employer to make the workplace “COVID-secure”



# Practical issues arising from the pandemic (4)

Employees may want to work remotely, abroad, for a prolonged basis. These working arrangements can create compliance, employment, regulatory and tax risks.



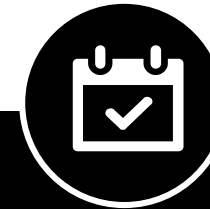
## Employment law

- Potential multiplicity of employment rights in different countries
- Employee might be able to cherry-pick most favourable rights/jurisdiction



## Tax

- Complex income tax and social security arrangements, dependent on place of residence / working time
- Specialist tax advice often required



## Compliance/regulatory

- Rules can differ by jurisdiction
- Rules can also be extraterritorial, e.g. for UK authorised firms, SMCR may apply to senior managers based overseas

## SMCR Resources

We have formed a multidisciplinary **SMCR Task Force** to help guide clients through the broad scope of legal issues brought on by this regime.

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To help keep you on top of developments as they unfold, we also have launched a resource page on our website at

<https://www.morganlewis.com/topics/uks-senior-managers-and-certification-regime>

If you would like to receive a daily digest of all new updates to the page, please visit the resource page to [subscribe](#) using the purple "Stay Up to Date" button.



## Biography



Louise Skinner provides sophisticated, strategic advice on all aspects of employment law, with particular focus on regulatory employment matters. Described as “truly exceptional and insightful” by clients in The Legal 500 UK guide, Louise advises on issues including investigations, contractual disputes, whistleblowing, discrimination and restraint of trade. Louise has particular experience in the financial services, life sciences, and sports, media and entertainment sectors.

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Chris Warren-Smith represents clients in investigations and disputes matters, including corporate investigations, commercial and international litigation and arbitration and dispute resolution, and regulatory enforcement proceedings. Representing clients across all sectors, Chris has worked on many high-profile issues and crises that have arisen over the years. He serves as deputy chair of the firm's white collar and corporate investigations practice and as a member of its global crisis management team.

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**Lee Harding, Partner**

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Lee Harding has a broad and versatile practice that goes beyond the provision of traditional legal services. Lee's practice is focused on the myriad legal implications arising out of a rapidly changing workplace: flexible working, five generations in the workplace, giving workers a voice, and the crossover between employment and the regulatory environment, to name but a few. The nontraditional legal services that Lee offers require a proactive approach to managing workplace issues before they escalate. He engages with a wide range of stakeholders to deliver sophisticated and actionable solutions that resonate across the entire business.

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## Biography



Steven Lightstone advises on financial services, securities, and derivatives regulatory issues. His clients include asset managers across a wide range of asset classes and their funds, banks, broker-dealers, fintech firms, payment institutions, institutional investors, insurers, lenders, and market associations.

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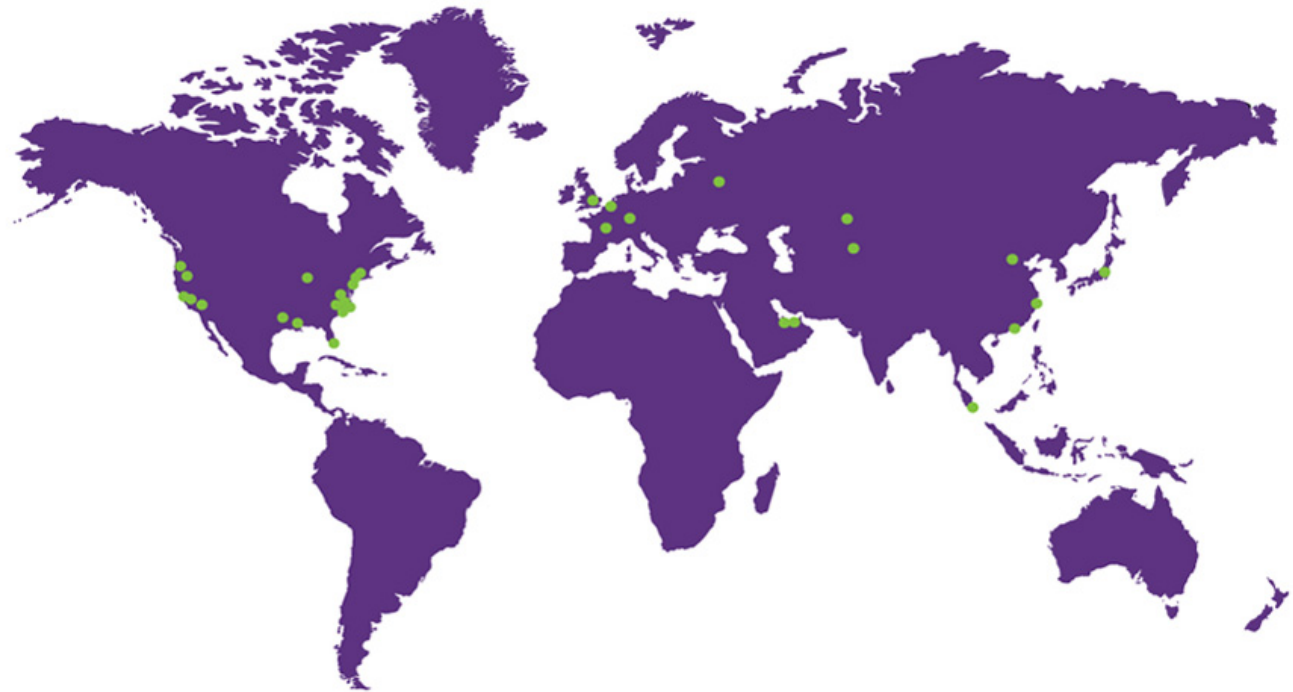
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